S. Hrg. 104–525

UNITED STATES POSTAL SERVICE REFORM: CONVERSATIONS WITH CUSTOMERS

Y 4. G 74/9: S. HRG. 104-525

United States Postal Service Reform...

HEARINGS

BEFORE THE

SUBCOMMITTEE ON POST OFFICE AND CIVIL SERVICE

OF THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTH CONGRESS

SECOND SESSION

MARCH 14 AND 18, 1996

Printed for the use of the Committee on Governmental Affairs

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UNITED STATES POSTAL SERVICE REFORM: CONVERSATIONS WITH CUSTOMERS

THURSDAY, MARCH 14, 1996

U.S. SENATE,
SUBCOMMITTEE ON THE POST OFFICE AND CIVIL SERVICE,
OF THE COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Committee met, pursuant to notice, at 9:30 a.m., in room 342, Dirksen Senate Office Building, Hon. Ted Stevens, Chairman of the Committee, presiding.

Present: Senators Stevens, Smith, and Dorgan.

OPENING STATEMENT OF SENATOR STEVENS

Chairman STEVENS. Good morning. Thank you very much for coming, gentlemen.

This morning we are convening the first of 2 days of hearings which my staff has called USPS Reform—Conversations with Customers.

The second part of our hearing will be held on Monday of next week at 2 o'clock in the afternoon. You all know how important the Postal Service is to the citizens of our country.

The 1970 act clearly and succinctly states that the basic function of the Postal Service is to provide postal services to bind the Nation together.

The communications network of the mail system is very important to all of us. In rural areas it is vital. In my State the Postal Service is literally a lifeline for most of our people. We depend upon the Postal Service for the basic necessities of life.

On July 1 of this year the U.S. Postal Service will celebrate its 25th anniversary, and we believe it is time for us to consider the future of the Postal Service and to work together to decide what tools it needs to continue well on into the next century.

Today and Monday we will hear from you who are the Postal Service customers, those people who really are very much involved in the mailing system.

We have asked that you describe how you envision the Postal Service of the future and the steps that can be taken this year by Congress to modernize that process.

I'm going to put the balance of my statement in the record today, because I do want to move along.

[The prepared statement of Chairman Stevens follows:]

Chairman STEVENS. I want to apologize now for the fact that I'm going to be called away for about 20 minutes during part of this

hearing to appear before another committee, and another Member of the Committee will be here.

We do hope that other Members of the Committee will come by and participate in this hearing. And I do appreciate the willingness of all of you to contribute to this process.

We have three panels of witnesses this morning, and I would like to ask that you put the complete text of your prepared remarks into our hearing record. We will put them all in there. Because of the number of witnesses, it would be helpful to maintain a 10-minute concept in the comments you make here this morning.

Our first panel consists of representatives of the Advertising Mail Marketing Association and the Direct Marketing Association. Both AMMA and DMA represent mailers who for the most part use what will be called the standard class of mail.

Testifying for AMMA is Ian Volner, the general counsel. Representing DMA are Jonah Gitlitz, the president, and he is accompanied by Mr. Baer of Reader's Digest, and Mr. McCormick from L.L.Bean.

Mr. McCormick. That's correct.

Chairman Stevens. We appreciate your coming and being willing to participate. Before we attempt to change the Postal Reform Act I think it is a very important thing for us to understand what you all feel about how the Postal Service should be reconfigured to meet your needs for the future.

Mr. Volner.

TESTIMONY OF IAN VOLNER, GENERAL COUNSEL, ADVERTISING MAIL MARKETING ASSOCIATION

Mr. Volner. My name is Ian Volner. I am general counsel to the Advertising Mail Marketing Association, and on behalf of all of our members we appreciate this opportunity to share with you our vision of what the Postal Service can become and the kind of changes practical, pragmatic, and relatively modest changes that needed to be made in order to accomplish that.

The basic theme of our view of the Postal Service is that the Postal Reorganization Act was a remarkable statute when it was passed. And it has endured quite well for 25 years. It was a good statute for its time, but times have changed.

Let us take a very brief look at what has changed. The Postal Service is, as you have said, first and foremost an information delivery system. In the past 25 years, alternative information delivery systems have sprung up all around it.

I'm not going to take you through all of the gory details of what has happened in the world around the Postal Service. We have set that forth in our statement.

But there is another element to this change in the world. The state of regulation of the alternative information delivery systems in this country has changed profoundly in the past 25 years. The Postal Service's state of regulation has not.

As a result of the 1996 Telecommunications Act there has been substantial relaxation of regulation of the electronic alternatives to the Postal Service. As a result of changes that Congress has made, UPS, FedEx, and other direct competitors of the Postal Service are now completely unregulated.

This relaxation of regulation—and I stress it is relaxation, not complete deregulation—has made these alternatives to the Postal Service flexible, market-driven and efficient.

We believe, it is our vision of the near future, that the Postal Service can become flexible, efficient, cost-effective and market-driven. The question is how to get there.

And I'm reminded of a story that Tony Frank told us once early on in his tenure. He was complaining somewhat indignantly that a Federal Government agency had assigned all of its overnight delivery mail to a competitor. He said they were not wrong to do that, their price is lower than mine. He said, "I can meet their price but it would take me a minimum of 10 months to get there." And quite understandably, the government agency didn't want to wait.

That is one area where change can be made, in the area of rate making and reclassification.

The other area, and the two are intertwined, is we need to do something to make more effective the Postal Service's dealings with labor, which represents something in the order of 80 percent of total costs.

Rate making can be made more flexible without sacrificing any of the important values that we have all agreed are necessary to bind the Nation together. I have had the misfortune of trying all of the rate cases that have ever been tried in the past 25 years, and a few of the non-rate cases that have been tried.

And it comes not just from my members, it comes from me. We have got to do something about the way rates are made. There are certain core values that we have to protect. We have to prevent predatory pricing. We have to prevent unfair cross-subsidies, except in the case of new services and incremental changes where there should be some time for the Postal Service to operate at a loss in order to start up a new service.

We have to protect universal service. That's important to your State, it is important to all mailers. And service has to be available to all users at reasonable costs.

But within those constraints, there is no reason that the Postal Service should be subjected to the kind of regulatory regime that it now undergoes.

It should be given, if not complete freedom, then a great deal more freedom than it has now to set rates, establish new services, to market tests.

We have listed all of the approaches that we believe can be quickly and easily accomplished in our prepared statement. There are two that I want to particularly emphasize because they are either mischaracterized or misunderstood by those who are opposed to any kind of change in the system.

We talk in our testimony about benchmark rate making. Essentially, benchmark rate making has been used in the telecommunications industry for almost a decade now. It has been entirely successful. It applies in monopoly markets, which the Postal Service will have, and it applies in competitive markets.

It does not mean that the Postal Service would be allowed to price below costs. What it does mean is if the Postal Service succeeds in controlling costs such that its aggregate costs do not exceed a benchmark, CPI, or some other determined benchmark, it

would not have to go through the 10-month ordeal that it now has to go through.

If the Postal Service cannot control its costs and it needs to increase its revenues from any class in excess of that benchmark, then it has to go through the whole ordeal.

The idea is you cannot mandate low rates. What you can do is provide the Postal Service with incentives to keep its rates down. And that's the notion of benchmarking. It provides incentive to control costs, and it leads to other things that I will get to in a moment.

The other proposal that we have advanced, which we believe to be profoundly important, is negotiated service contracts. Again, this is not a revolutionary idea. It has been employed in the telecommunications field for more than a decade.

It doesn't mean that big mailers would get below-cost rates and everybody else would pay. It doesn't mean the end of universal service.

What it means is that if a mailer is willing and able to make certain commitments to the Postal Service, such as not delivering his mail at the wrong time of day, or refrain from mailing during certain days of the week so that the Postal Service can more efficiently manage its workload, and thereby save all of us money, that mailer would get something of a rate break.

It does not mean unregulated rates, because the negotiated service arrangement would have to be approved by the Postal Rate Commission. There is nothing terribly radical in this. It has been looked at by a half a dozen courts. It has been found to be perfectly lawful, and I can tell you from personal experience it works extremely well in the telecommunications field, not just for large mailers. In the present environment, an individual consumer can get 800 toll free service at home. And that's a direct outgrowth of what they call individual case-based tariffs, and what we call in the postal world negotiated service arrangements.

These are things that can be done. Some of these are things that can be done without legislation. But we have been discussing these matters for a decade, and it is time to get on with it. And what we are asking the Subcommittee to do is to help us frame legislation to get these kinds of rate flexibility procedures into place so that the Postal Service cannot only meet its competition, but also serve all of us and preserve the core values that we all share.

The other side of the equation is managing Postal Service costs. It is abundantly clear that costs drive rates, and it doesn't do any good at all to change the rate structure unless we also provide some mechanism—better tools, to use the Senator's phrase—to deal with the management of costs.

Any more than you can't legislate low rates, you cannot legislate low costs. What we can do is provide the Postal Service at all levels—and I want to stress that, at all levels—with incentives to keep their costs down.

Benchmark rate regulations provide them with one incentive. It means you don't have to incur the expense and the pain and the bother of 10 months of ordeal, with results that are never entirely satisfactory to anybody.

There are other incentives directly on the labor side of the equation, however, that we regard as very important.

Again to invoke Tony Frank, he pointed out early on in his tenure that the problem with a Postal Service craft employee is that if he works eight hours and completes his work in less than eight hours, he gets more work to do. If he completes his work in more than eight hours, he gets overtime. The only way that an employee in the current system can earn more money is not to increase productivity, but to decrease productivity. That's not logical.

Incentives have to be provided so that all employees, from management on down, want to succeed, want to increase productivity, want to deliver the mail better, faster, more cost controlled, and in ways which are more responsive to the needs of their customers.

The other side of the equation from the overtime example is this past year the Postal Service posted a surplus of $1.5 billion, or some such number. And they were able to hand out $12 million in bonuses to their employees, to the management level, senior employees.

Because of the salary caps, some of the senior-most people got a bonus of $500. It ought not to stun us that there is a lack of incentive, a lack of risk taking on the part of Postal Service Management. If all I have to gain is $500, why take the risk, let's just rock along. The system functions. It is in fact the best system in the world. And let's not worry about whether it can be better because there is no reward in it for me.

So we believe that we need incentives on both sides of the equation, management and labor. We also believe that there is a way of producing a reality check and ending once and for all the interminable debate about whether Postal Service employees are over or underpaid. It is called out-sourcing.

About 10 percent of the Postal Service's total budget is expended on contracting out. There are no ground rules, and the efforts to contract out have not been successful.

The Congress needs to supply ground rules telling the Postal Service when and where it can contract out, and requiring the Postal Service to allow its incumbent union employees to bid on those contracts.

From the mailers perspective, we don't care who carries the mail or who processes it or who sorts it. What we care about is that the price that is paid by the Postal Service for that function be fair and competitively arrived at. Allowing the unions to compete with private sector companies for contracting out functions accomplishes that goal.

So we are not asking for a lot. It is just those two areas that need to be addressed, and we believe that in those two areas change can be made this year in ways which preserve the basic values that we are all trying to preserve.

I don't want to sound overly dramatic in ending, and I'm not sure that this is politically correct but I'm going to adapt it anyway. This debate about what we should do about the Postal Service has been going on now for several years, and I am reminded of Bobby Kennedy's line, "Some people see the world as it is and ask why." We at AMMA see the world as it can be and ask why not. And the why nots are in those two areas, and it is not hard to fix.

Thank you very much.

[The prepared statement of Mr. Volner follows:]

PREPARED STATEMENT OF IAN D. VOLNER ON BEHALF OF THE ADVERTISING MAIL MARKETING ASSOCIATION

INTRODUCTION

The Advertising Mail Marketing Association (AMMA) appreciates this opportunity to share with the Subcommittee our views on the need for modernization of our Nation's postal system. We believe that the U.S. Postal Service faces serious challenges, but that the problems it faces and will face in the coming decades can be overcome. We welcome and endorse the Chairman's announced intention to introduce legislation by mid-year that takes the first step toward modernization. The Postal Reorganization Act of 1970 was well designed for its time, but times have changed. The American public needs the help of this Subcommittee, so that today's problems are overcome and the challenges of tomorrow are met.

Our call for legislative and regulatory reform proceeds from a simple premise. This Nation needs and will continue to need a universal mail delivery system. To satisfy that need, the postal system must become a market-driven, flexible, cost-effective provider of timely mail delivery services.

That is our vision. It is not the present day reality. We believe the Postal Service can become all of the things that the public deserves. However, that will require changes in the legislative and regulatory structure under which the Postal Service operates and transitional devices to enable the Postal Service to move smoothly and orderly to what it can become.

Our assessment will be too modest for some and not modest enough for others. To paraphrase Winston Churchill's immortal words, AMMA does not regard the legislation this Subcommittee is contemplating as the end, or even the beginning of the end; we do regard this legislative initiative as the end of the beginning. Our purpose is, as the Subcommittee has asked, to suggest practical and moderate ways in which our vision of a market driven, flexible Postal Service can begin to become a reality.

EXECUTIVE SUMMARY

Across all of its modern core businesses—business-to-consumer and consumer-to-business mail—the Postal Service faces competition from direct competitors and alternative, electronic, information delivery systems. Deregulation of alternative delivery systems (such as UPS), technological advances in the telecommunications field and the recent passage of the 1996 Telecommunications Acts have promoted services which are market-driven, cost-effective and flexible. The Postal Service cannot vie for business against these alternatives under a statute which stifles innovation, creativity, and responsiveness. The Postal Services faces loss of market shares and a downward spiral of relentlessly increasing rates and loss of business.

AMMA wants legislative and regulatory reform. This means that:

- The Postal Service must be enabled to set rates that reflect the competitive market in which it operates. Pricing standards which ignore or underestimate demand considerations are a recipe for disaster in a competitive market. Yet, that is how the 1970 Act is applied. The rate setting criteria must be replaced. Consideration should be given to adoption of benchmark rates, which insist upon cost control and allow the Postal Service to reflect differences in demand in its rates. The Postal Service must also be allowed to customize its service offerings, to test new products and fine tune rates for changed products. No rational business can operate under constraints which permit the introduction of new services only if they are instantly profitable. This makes it very difficult to test new market opportunities, and virtually forces a feast-then-famine cycle of rate increases, surpluses, operating losses and yet more rate increases. While the Postal Service has not used the flexibility that the law now allows, it needs to be encouraged to innovate and be provided with flexibility it needs to thrive, not merely survive.

- There is need for incentives for success at all levels within the Postal Service. The legal structure of the Postal Service's personnel policies is characterized, from top to bottom, by a lack of the incentives consistent with an enterprise that must conduct its affairs in a competitive marketplace. It is impossible for the Postal Service to reward exceptional performance, and it has been unwilling or unable to sanction grossly inadequate performance. The absence of incentives is paid for by the public through service problems, automation difficulties, and modernization delays. The entire structure of labor relations

must be examined with one question in mind: Is the statute, rule or policy conducive to an enterprise in which employees succeed because they are rewarded for success? There are several modest changes in the law (including clear rules regarding outsourcing) which will advance that goal.

- The Postal Service must actually compete. Whether or not the monopoly is removed or relaxed, the law must be changed to make clear to the Postal Service—at all levels—that it is no longer enough to act "as if" the Postal Service had competition. It must be competitive.

AMMA is convinced that, in an orderly and rational fashion, the Postal Service can become what it must become—market-driven, cost-effective, flexible and timely.

REDEFINING THE VISION: THE CHANGING ROLE OF MAIL IN AMERICA

1. *The 1970 Vision of The Postal Service Is Obsolete.* The 1970 Act defines the mission of the Postal Service in the following words:

> "The Postal Service shall have as its basic function the obligation to provide postal service to bind the Nation together through the personal, educational, literary, and business correspondence of the people."

This formulation of the Postal Service's mission as one that "binds the Nation together" goes back to the founding of the Republic. This mission remains sound. But, the composition of the mailstream has changed markedly, and the means of accomplishing this mission must therefore be changed.

What the Postal Service actually delivers today bears little resemblance to the 1970 mission statement. Let us look at what has happened to "business correspondence." The Postal Service has estimated that, over the past 5 years, it has lost approximately 35 percent of the business-to-business transaction market. The telephone, facsimile, EFT, EDI and electronic mail are increasingly providing functions formerly provided by mail alone. With the increased deployment of integrated services digital networks it is very likely that this trend will continue and accelerate. Indeed, the Postal Service estimates that it will lose an additional 35 percent of the business-to-business financial and transaction market over the next 5 years. Business-to-business mail is no longer the engine that drives the postal system.

Let us consider, then, "personal correspondence." The notion that the primary purpose of the Postal Service was to deliver personal correspondence—invitations, greeting cards, and personal notes—was, at best, uncertain in 1970. It certainly is untenable today. According to Postal Service studies, only 6 percent of total mail volume in 1994 constituted personal correspondence. There is nothing astonishing in this: 98 percent of the American public receive telephone service. The introduction of competition over the past three decades has made telephone service and equipment cheaper and far more easy to use—for personal as well as business purposes—than it was 25 years ago. Personal correspondence will remain a part of the Postal Service's role in the years ahead. Nonetheless, in 1995 it cannot be said that the function of the Postal Service is, first and foremost, to deliver personal letters and the like.

The Postal Services "core business" today is to deliver correspondence that invites and completes consumer transactions. It is the American consumer, and the companies serving them, that are threatened by the competitive crunch the Postal Service faces.

2. *The Competition Crunch.* There can be no guarantee that the Postal Service will be able to retain the strength that it possesses in its modern core business. Even with its monopoly, the Postal Service has lost revenues to direct competitors and other forms of information delivery. Unless steps are taken, that erosion of market share will continue. It will carry with it a spiral of increased rates and increased diversion. In the past decade, rates for advertising mail have increased by more than 80 percent. AMMA's members cannot endure future increases of this magnitude, and are unlikely to sit by passively as other—particularly electronic—means of delivering their messages become more readily available.

Twenty-five years ago, home shopping television did not exist because of federal regulatory constraints. Those policies were repealed in 1983–1984. Television home shopping has since grown into a multibillion dollar a year business. We can learn from this. Deregulation does create new opportunities, and that can be as true for the postal system as it has been for television. Conversely, the Postal Service can lose revenues to other information delivery services. It undoubtedly already has lost some to home shopping. It will lose more—and quickly—if its rates continue to escalate as they have over the past decade.

Parts of the Postal Service's core business are also challenged by telemarketing. By some estimates, as much as 40 percent of AT&T's total long distance revenues are attributable to 800 number telephone calls. Consumers find 800 service an easy, cost effective means of satisfying their needs and wants. It is perfectly plain that 800 number service is a close substitute for the Postal Service's business reply mail, and the recent introduction of a new toll free code will increase the usage of this service. In no small measure, the growth of telemarketing is due to the introduction of competition and the corresponding relaxation of regulation in the telephone field. In ways which are utterly impossible in the current postal environment, telephone marketers are able to negotiate with their long distance telephone carriers to achieve economically efficient operations. The introduction of competition in local exchange service mandated by the Telecommunications Act of 1996 will further extend flexibility to local business activities.

Online interactive services have been stimulated by the technological and regulatory changes that have occurred in the telecommunications field. These, too, are growing at remarkable rates. It is projected that 40 million households will have access to these services by 1998. That puts this delivery system in the same league as cable television. And consumer use of the direct marketing applications of interactive, online service will grow with it.

Further, the fact that consumers predominately use mails for payment of their bills today is not proof that they will do so tomorrow. Indeed, the evidence is to the contrary. Alternative, non-postal methods of payment abound. Automated teller machines ("ATM") have achieved true ubiquity. Bank-by-phone options are offered by all major financial institutions. The passage of the Electronic Funds Transfer Act and changes to the banking rules have also opened up methods of hard copy payment—automated check generation systems—to consumers that either cannot qualify for or do not wish to have credit or debit cards; these transactions typically bypass the Postal Service. In 1994 the Postal Service reported a small, but ominous, decline in mail (mostly payments) from households to businesses.

This, then, defines the impending challenge. A delivery system which is, itself, not market-driven, not cost-effective, not flexible finds itself facing direct competitors and alternative information delivery services that are.

Ours is not an apocalyptic vision. We believe that the Postal Service can do well in the electronic age. Radio has not replaced the newspaper. Television has not supplanted radio. Cable television and its multichannel competitors have not obsoleted over-the-air television. The Internet exists side-by-side with plain old telephone service. However, each one of these forms of information delivery, including plain old telephone service, have changed in the ways in which they seek to serve their markets. They will further change and evolve as the result of the recent overhaul of the Communications Act.

The Postal Service must also change—redefine its mission, its pricing strategies and the way it operates. It cannot do so today because of unnecessary and artificial legal and regulatory barriers. Those obstacles must be removed in an orderly and rational fashion.

ENABLING THE POSTAL SERVICE TO FILL ITS MODERN MISSION: THE OBSTACLES AND THE SOLUTIONS

The Subcommittee has asked us to identify three specific areas in which steps should be taken this year to begin the process of modernization. We strongly believe that legislative change of a statute that is now 25 years old, and no longer in touch with the realities of the modern marketplace is necessary in three areas: (a) Matters of Rates and Services, (b) Matters of Labor Relations and Costs, and (c) Matters of Competitive Operations. We deal with each of these in turn.

MATTERS OF RATES AND SERVICES

1. *The Postal Service must be permitted to set rates that reflect the competitive market in which it operates.* There is a profound disjuncture between economically efficient rates and rates which Postal Rate Commission believes proper. The Commission's prevailing view is that rates must be "fair and equitable" largely without regard to the ability of the Postal Service to compete in its modern core areas of business. Indeed, the Office of Consumer Advocate—appointed by the Commission under the statute to represent "the public"—has explicitly stated that it would be "sheer coincidence" if rates were "fair" and also reflective of mailer demand.

Pricing which ignores or underestimates marketplace realities in a competitive environment is a recipe for disaster. This is not just the view of AMMA and its members. The GAO has, not once but twice, criticized the Rate Commission for its refusal to give proper weight to demand considerations in its review of postal rate pro-

posals. Mail for which the Postal Service could compete on price terms and which is, ironically, among the most "profitable" to the institution—because of its contributions to overhead costs—is denied to the Postal Service on the apparent theory that to do otherwise would not be "fair and equitable" to other users of the system. This pricing theory may also reflect wrong-headed "social policy" designed to redress or restore the "purity" of the Postal Service's mission as it stood in 1970.

The rate making criteria must be changed. We are not suggesting that the Postal Service should be permitted to price services below cost. For so long as the Postal Service maintains a monopoly, there must be appropriate safeguards against predatory pricing and cross-subsidization of competitive services from revenues received from captive mailers. Direct costs should be the floor on rates for all services, except new, incremental or experimental services. We are suggesting that the notion of some free floating "fairness and equity" principle which enables regulators to ignore the competitive challenges and opportunities the Postal Service faces is bad policy. When that standard operates, as it does in the competitive environment confronting the Postal Service, to the detriment of those it is supposed to protect, the time has come for change.

One way of enabling the Postal Service to sensibly and fairly price its products is to replace cost-of-service rate making mandated by the 1970 Act with a form of rate regulation based upon "benchmarks". Under benchmarks regulation, direct cost would remain the floor on rates, but the Postal Service would be permitted to otherwise change its rates with minimal regulatory review so long as the aggregate increase does not exceed an objective limit, such as the CPI. Implementation of benchmark rates will require the establishment of baseline rates that more closely correspond to market conditions than rates now in effect. However, once this is accomplished, benchmark regulation would end the debate over whether rates can be "fair and equitable" and also economically efficient. This rate making standard insists on cost control and at the same time allows rates to reflect the differences in mailer demand for different postal services. This approach to rate regulation is widely used in the telecommunications field, in monopoly as well as competitive environments. It is being deployed by other postal administrations, and it deserves serious consideration here.

2. *The Postal Service must have the flexibility to fine tune rates, test new products and customize service.* Another anomalous quality of the Postal Reorganization Act is that it invites the feast-then-famine cycle of omnibus rate increases followed by periods of surplus, followed by operating losses and more omnibus rate cases that have characterized the past 25 years. This virtually compels the use of accounting gimmicks in connection with regulated rates—including the contingency reserve and the recovery of prior year losses—which pad rates at the front and back end of the cycle. Benchmark rate regulation would enable the Postal Service to fine tune rates to meet changing conditions without recourse to the endless cycle of omnibus rate cases, to accounting gimmicks, and without recourse to the feast then famine approach to break even that is now employed.

Also, the introduction of new or altered services is exceedingly difficult under the "break-even" requirement, as it is now employed, unless it can be shown that a new service will, from its inception, fully recover costs. No rational business can operate under this constraint. The Postal Service is either unable or unwilling (or both) to market test new or changed offerings under the current rules. This can and must change.

Lastly, the Postal Service should, subject to appropriate safeguards, have the right to enter into Negotiated Service Arrangements—sometime called customized tariffs—with customers who are able and willing to configure their mailings and mail in ways which enable the Postal Service to better control its workload and to process and deliver mail efficiently. Such arrangements are widely, and very successfully used in the telecommunications field. One of the difficulties with the Rate Commission's view of the Postal Reorganization Act is the belief that policies which are good for large mailers must definitionally be bad for smaller users of the system. Experience within and outside the postal field proves otherwise.

These ideas have been discussed for almost a decade. Not all of these changes require legislation. But, nothing has happened; and it is increasingly clear that the changes the Commission is willing to make are, at best, half-measures that stop short of giving the Postal Service the flexibility it needs. The Commission seems to hold to the view that, until volumes of mail actually and aggressively are lost to competitive alternatives, there is no need for change. That strategy was followed by Western Union and its regulators the 1970's. By the time Western Union awakened to the competitive threats it faced, it was too late. Congress should not permit that to happen to the Postal Service. The need for greater flexibility in the introduction of new services, market testing and in the creation of customized service agreements

subject to appropriate but limited safeguards is readily apparent. If the statute needs to be changed to create greater flexibility in rate adjustments and the introduction of new services, then the appropriate changes should be made.

MATTERS OF LABOR RELATIONS AND COST

Plainly our vision of a market driven cost effective system will not become reality unless the Postal Service is given better means to control its costs. Costs drive rates and no amount of tinkering with the rules of rate regulation will make the Postal Service cost effective with inadequate and outmoded cost controls.

The inadequacies of the legal system governing Postal Service personnel cut across all segments of its workforce. The salary caps, commanded by law, operate from the top down. Both labor and management express dissatisfaction with the collective bargaining process and with the proliferation of grievance hearings that characterize day-to-day management. It is virtually impossible for the Postal Service to adjust the size of its workforce through voluntary retirements. It is, more importantly, very difficult for the Postal Service to reward exceptional performance—at any level. As a corollary, the Postal Service has been unable or unwilling to sanction grossly inadequate performance except through measures—such as transfers—which are not solutions.

This absence of incentives to excel is paid for by the public—businesses and consumers alike. We have and will continue to pay for the decisions of the Merit System Protection Board, regarding the Postal Service's effort to right-size itself. We pay for the Postal Service's inability to capture all of the benefits of automation. We pay for system failures. That there will be occasional system failures even in the best run enterprises must be accepted. That the Postal Service is too often slow to detect and respond to system failures is at least in part directly attributable to strictures of the legal system. That cannot be accepted.

It is necessary, then, that the entire legal structure of labor relations in the postal system be examined with a clear eye and one question in mind: Is the particular statute (or policy that has developed underneath it) conducive to an enterprise that is market driven, cost effective, flexible and in which employees succeed because they are rewarded for their success?

This question can and must be resolved in ways that work for employees and managers alike. There are several specific provisions of the Reorganization Act that need to be changed to satisfy both of these interests. First, the salary caps need to be removed or, at the least, substantially increased, so that the Postal Service can more readily attract and keep first-class managers and leaders. Second, surpluses earned under benchmark rate regulation should be shared with all employees, so long as certain financial and performance goals are met. Last year, the Postal had a surplus of more than $1.5 billion; it was able to hand out bonuses to key employees of less than $12 million, and some of the senior most people—who most contributed to the Postal Service's success—received bonuses of less than $500. It ought not to be surprising that many managers in the system are unwilling to be creative, innovative and responsive to customer needs. There is little incentive for them to do so.

Rewards must also be available to unionized employees. Under the present system, it makes little difference to craft employees whether the Postal Service does or does not meet its productivity and financial goals; the only way a craft employee can increase his or her income is through overtime. It ought not to be astonishing that the Postal Service has chronic problems with productivity and has never been able to fully capture the cost benefits of automation. All employees should be given the incentive to succeed and the rewards of their success when they are earned.

Three of the last four Union Contracts went to binding arbitration. Arbitration is conducted under a vague standard which requires that postal wages and working conditions be "comparable" to those in the private sector. As might be expected, the Postal Service and the Postal Unions have not and probably can never agree on what that phrase means or how it is to be applied. The standard for wage setting and the formulation of work rules must be changed to reflect the fact that the Postal Service faces competitive challenges so that labor negotiations more closely replicate those that occur in the private sector, including incentive rewards.

One way of accomplishing this is to clarify the law as it relates to outsourcing of the Postal Service's core functions of processing and delivering mail. About ten percent of the Postal Service's budget is contracted out to private sector firms. As the GAO has pointed out in several of its reports, the rules that determine when the Postal Service may contract out its functions to private sector firms are very poorly defined, and this has inhibited outsourcing. At least one major contracting out initiative—the remote video bar-coding project—collapsed, and the work was

brought in-house, (at considerable cost to the Postal Service and ultimately mailers) because of this lack of ground rules. Congress should define the circumstances in which the Postal Service is permitted to contract out. However, the statute should permit the Postal Unions, or their bargaining units to bid—along with private sector firms—for this work outside of, or in addition to, the basic wage package. What matters is not who performs the work, so long as it is performed competently and at a labor cost that is competitive. Allowing the Unions to bid on outsourcing projects provides assurance that key functions will be costed—and therefore can be priced—competitively.

MATTERS OF COMPETITIVE OPERATIONS

When he took office, then Postmaster General Frank announced that, although legally protected from competition, the Postal Service had to act "as if" it had competition. That was nearly a decade ago; and it is clear that the "as if" strategy has not worked. Too often, the Postal Service denies or just ignores service and operating problems that are readily apparent to those with whom it deals. It remains slow to respond to customer needs and concerns. It still suffers from a Not Invented Here Syndrome which leads it to reject any innovation that does not originate within the Postal Service itself. It has proved either unable, or unwilling, to avail itself of the limited opportunities for rate and service innovation the Rate Commission has provided to it.

This will not do. If the vision of a market-driven, flexible, and responsive Postal system is to become a reality, the corporate culture of the Postal Service must change, and change profoundly. Of course, Congress cannot legislate a change in corporate culture. It can, and it should, hand the Postal Service the tools, subject to appropriate but limited safeguards, to transform its culture. The legislative changes we have outlined above will, we believe, enable the Postal Service to actually become competitive.

AMMA recognizes that the legislation the Subcommittee is contemplating may be only the first step in that process. There are those who say that the Postal Service will never become truly competitive unless the monopoly is repealed. Certainly, the importance of the monopoly in the modern environment needs to be studied, and not just by the academics and the think tanks but by the Postal Service itself and those who deal with it. Certainly, if—as we expect—the more modest changes we have proposed are successful, the need for a Rate Commission, at least as it is currently structured and constituted, must be re-examined. But there are examples of non-commercial organizations that are protected by a monopoly but are also very effective and responsive to public needs. It would be a grave mistake for Congress to take no steps towards modernization of the Postal Reorganization Act because some longer range solutions are complex and therefore controversial.

We recognize that some of the measures we have advocated in this testimony will themselves be regarded as extreme by those who compete with the Postal Service or perceive themselves as competitors and by those who are content with the status quo either because they do not realize the importance of the challenges the Postal Service faces in the modern marketplace. We think it would equally be a mistake for Congress to take no steps toward modernization of the Postal Reorganization Act because even modest proposals generate some controversy.

CONCLUSION

If we have learned nothing else in recent years, it is that the Postal Service simply cannot become a truly market-driven, effective and efficient provider of information delivery under a statute that was well designed for its time, but is now 25 years old. With some help from Congress we believe that the Postal Service can transform its corporate culture in ways that make the vision of what mailers need to begin to become a reality.

Chairman STEVENS. Thank you very much, Mr. Volner.
Mr. Gitlitz.

TESTIMONY OF JONAH GITLITZ, PRESIDENT, DIRECT MARKETING ASSOCIATION

Mr. GITLITZ. Senator, thank you so much. I'm Jonah Gitlitz, president and CEO of the Direct Marketing Association. It is an honor to be presenting DMA's views before you this morning.

I would also like to add that over the years we have certainly respected the fairness with which you have approached these issues.

With me today to present the views of two distinguished DMA members companies are Cary Baer, vice president, U.S. Delivery Services of Reader's Digest, and Chris McCormick, senior vice president in advertising and direct marketing of L.L.Bean.

I would also like to acknowledge the presence in the room this morning the chairman of DMA for this year, Robert Edmond, and I think you have met Mr. Edmond.

DMA, as you know, represents over 3,600 companies, of which over 3,200 are U.S. companies who offer goods and services directly to the public through a variety of media.

In the United States, direct marketing represents over $1.1 trillion annually in revenue and employs over 19 million Americans, according to a recent economic study conducted for us by the WEFA group.

Our members use all forms of communications media, but certainly the major medium traditionally, certainly up to this point in economic history, is the significance of the U.S. mail to direct marketers.

The vitality of this growing industry depends significantly on the performance of the U.S. Postal Service, so postal reform is a very significant issue for us, and has been for many years.

We have certainly strongly supported the efforts of Post Master General Marvin Runyon to bring costs under control and to position the Postal Service to be an effective player in the increasingly competitive communications market. We think he has done an excellent job, but certainly much remains to be done.

One of the needs is to reform the legislative framework in which the Postal Service operates. Direct marketers require really three things from the Postal Service, or any other hard copy delivery service: Universal delivery to every household and business in America, reliable and timely service, and reasonable prices.

The Postal Service certainly meets the first two requirements well. Certainly over the years there have been periodic concerns with delivery problems, but overall we would have to say that direct marketing messages reach customers and potential customers within acceptable standards for deferred delivery of advertising mail.

As for the third leg of the stool, the Postal Service, however, must recognize that a reoccurrence of the staggering rate increases of the 1980s and early 1990s will greatly affect its future in the new information age. You will be learning soon from Chris McCormick that postage costs for L.L.Bean catalogs have increased over 90 percent since 1988.

The postage rates for both third-class advertising mail, soon to be named standard mail, as we know, have increased on average 66 percent over the past 10 years.

Over the years, DMA and many of its members have raised their voices to complain about the PRC, that it has not treated bulk third-class mailers fairly because it increased third-class rates proportionally much higher than other classes.

However, we all recognize that the underlying cause of spiraling postage rates is the inability of the Postal Service to control its costs.

The GAO tells us that postal productivity has improved very little, despite billions of dollars spent on new plants and equipment, including new automation equipment.

GAO has testified numerous times that the USPS has failed to capture the savings projected for the automation program. The Postal Service cannot hope to survive in the new information age if its cost-cutting programs are failures.

Now, the new mail classification system, which the government has accepted this month, and which becomes effective July 1, is the next step and offers a great opportunity to attempt to trim and cut and control costs. DMA and other third-class mail users supported the Postal Service before the Postal Rate Commission. It is now the duty of postal management to make this work, to reap the rewards of the new automation compatible mail classification, and to pass the savings on to mailers. It productivity does not dramatically increase as a result of these efforts, the prospect for survival, we think, of the Postal Service as we know it are bleak.

Now in the face of new technology and alternate media that will be described later this morning, rising postal rates will force all mailers to curtail their use of the mail as they attempt to cut costs. And that is happening. The PMG has stated clearly in recent months that the Postal Service is losing its market share in the communications of our great Nation as a result of new technology and old competitors.

Even worse, postal mail volumes of the past few years have grown significantly less than the growth of the overall American economy, and less than historic mail volume growth. And we all know what happens when volume is stagnant or declining. It is a cycle. The costs of the universal delivery network fall on fewer and fewer pieces of mail, which in turn increases the cost of mail delivery, which increases rates, which causes further questions about mail volume.

Moreover, the first mail volumes to leave the system are usually the least expensive for the Postal Service to process. For example, the loss of third-class volume would eliminate or reduce its $3.36 billion contribution to overhead costs, which would require other users of the service to cover the cost of lost funding. Rates simply go higher and higher.

Now, in our view the new communications media in the information age can complement existing media, not necessary replace them. For business mailers, we see the new media as adding to the market mix, again not necessarily supplanting existing media. For mail, of course, and for the Postal Service, this assumes that rates and service are competitive. Mail volume should be growing at a robust rate, and the Postal Service must control its costs.

Moreover, consumers, our customers, would be adversely affected by spiraling postage rates. Research indicates, again, that the American public enjoys receiving mail and information on products and services available to them. The growth of our industry, that we refer to above statistically, is based on consumer acceptance.

Now, how can the Postal Service control its costs? After months of discussion, arguments, and certainly more discussion among our members, DMA believes that the best path to achieve postal cost reductions in the long run is through the discipline of competition. Competition, and the potential for failure, will give all of those involved in the Postal Service a sense of urgency to control costs and become more competitive in the communications market.

However, immediately moving into a truly competitive environment for the U.S. mail would wreak havoc on every industry dependent on the service. Neither the USPS nor its present and potential competitors are ready to switch to an open market for a business delivering over 180 billion pieces of mail, with $55 billion in annual revenues.

Direct marketers and the Americans employed to support them could not withstand even a 1 month disruption in the universal hard copy delivery system. Any move toward competition, therefore, must be phased in, allowing the Postal Service, its employees, the mailers and competitors, adequate opportunity to adjust and prepare.

So, Senator Stevens, we applaud your request to each witness at these hearings for suggestions of postal reforms which could be enacted this year.

Moving directly to competition is not one of them. However, we do believe that there are other steps that can be taken and should be taken first.

DMA believes that if the Postal Service were given more flexibility over rates and classification, it would have more tools to enable it to control costs and improve its financial viability.

Attached to my testimony is draft legislation to give the service that flexibility. Many of the provisions in the attached draft were crafted in discussions among mailers, postal employee organization, and the Postal Service itself 4 years ago. We have updated some of those recommendations.

As you can see, this subject has been around for many years. We have updated the proposals again, and believe they represent an appropriate basis for discussion of the first steps in postal reform legislation.

And briefly, the draft legislation would, again, allow the Postal Service to adjust rates without a rate proceeding at the Postal Rate Commission, if USPS costs, as defined by the PRC, are below the rate of wage inflation. All rates would be changed by the same proportions, and rate increases would be restricted to 75 percent of the employee compensation index.

There is a role for the Postal Rate Commission, and we point out that rates could not be adjusted under this section for more than 5 years after the PRC recommended general rate change, and the Postal Service would have to certify to the Postal Rate Commission its reasons for increasing these rates. So there is a role for the PRC in this.

Second, we provide that the entire Board of Governors, not just the nine presidentially appointed governors, vote on all Postal Rate Commission recommendations. The full board also consists of the PMG and the Deputy PMG, who are selected by the governors. We

believe that they too should have a vote in this critical area of rate making.

We also provide that a three-fourths majority of the Board of Governors may modify a further recommended decision of the Postal Rate Commission, rather than the unanimous vote now required; allow the Postal Service to test experimental service offerings without seeking a PRC recommendation, provided the experimented is limited in both scope and duration. And it is important to note that Chairman Glyman and the PRC are moving in this direction right now in their own rule making, and we encourage and support them in this effort.

Allow the Postal Service to change mail classifications which do not change rates through notice and comment rule making. Allow the Postal Service to make limited changes in the nature of postal services through notice and comment rule making. Provide subpoena power to the PRC for Postal Service documents and data specifically related to rate and mail classification case issues to help eliminate any delays caused by the failure of the Postal Service to provide the Commission the information it needs for deliberations.

And finally, to impose a deadline on PRC reconsideration of any recommended decision returned by the governors. Our draft legislation also provides for increased compensation for governors, similar to the provision sponsored by you, Senator, earlier this Congress.

We would suggest that these salaries be adjusted from time to time to reflect inflation. The draft also allows for bonuses for senior postal management that could exceed the statuary limit for compensation of postal officials. Ian referred to that earlier very eloquently.

These two provisions are designed to improve the ability of the Postal Service to attract and retain qualified managers and governors.

The draft legislation grants the Postal Service much of the freedom it has been requesting for the past 5 years. It represents a first step in postal reform. How well the Postal Service performs with its new freedom will dictate both the content and the timing in the next step in the reform process.

DMA urges you, Senator, and the Committee to give postal management more freedom and to hold them accountable for the results of their actions under their new freedom.

Again, it has been a great privilege to be asked to testify before you today. I'd be pleased to answer any questions you have.

Let me now move along and introduce Chris McCormick, who is senior vice president, Advertising and Direct Marketing, of L.L.Bean.

Thank you.

[The prepared statement of Mr. Gitlitz follows:]

PREPARED STATEMENT OF JONAH GITLITZ

Senator Stevens, distinguished Members of the Committee. I am Jonah Gitlitz, president and chief executive officer of the Direct Marketing Association, Inc. It is an honor to be asked to present DMA's views on reform of the United States Postal Service. With me today to present the views of two distinguished DMA member companies are Cary Baer, vice president of US Delivery Services, Reader's Digest,

and Chris McCormick, senior vice president, Advertising and Direct Marketing, L.L.Bean.

DMA represents over 3,600 companies, of which over 3,200 are U.S. companies, who offer goods and services directly to the public. In the U.S. direct marketing represents over $1.1 trillion annually in revenue and employs over 19 million Americans. Our members use all forms of communications media to contact their customers and prospective customers. Traditionally, one of the major, if not the major, medium for direct marketers is the U.S. Mail. The vitality of this still-growing industry depends significantly on the performance of the United States Postal Service. Postal reform is a subject near and dear to the hearts of direct marketers.

We have strongly supported the efforts of Postmaster General Marvin Runyon to bring postal costs under control and to position the Postal Service to be an effective player in the increasingly competitive communications market. He has done an excellent job, but much remains to be done. And one of the needs is to reform the legislative framework in which the Postal Service operates.

Direct marketers require three things from the Postal Service or any other hard-copy delivery company:

1. Universal delivery to every household and business in America;
2. Reliable and timely service; and
3. Reasonable prices.

The Postal Service meets the first two requirements well. Over the years there have been periodic concerns with delivery problems, but overall, direct marketing messages reach customers and potential customers within acceptable standards for deferred delivery of advertising mail. As for the third leg of the stool, the Postal Service, however, must recognize that perpetuating the staggering rate increases of the 80's and 90's will greatly affect its future in the new information age. As you will learn from Mr. McCormick, postage costs for L.L.Bean catalogs have increased over 90 percent since 1988. The postage rates for bulk third-class advertising mail, soon to be named Standard Mail have increased on average 66 percent over the past 10 years.

Over the years DMA and many of its members have raised their voices to complain that the Postal Rate Commission has not treated bulk third-class mailers fairly because it increased third-class rates proportionately much higher than any other class. However, we all recognize that the underlying cause of spiraling postage rates is the inability of the Postal Service to control its costs. Postal productivity has improved very little despite billions of dollars spent on new plants and equipment—including new automation equipment. GAO has testified numerous times that the Postal Service has failed to capture the savings projected for the automation program. The Postal Service cannot hope to survive in the new information age if its cost cutting programs are failures.

The new mail classification system which the Governors accepted this month, and which will become effective on July 1, 1996, is the next step in the Postal Service's automation program—its major attempt to cut costs. DMA and other third-class mail users supported the Postal Service before the Postal Rate Commission. It is now the duty of postal management to reap the rewards of the new automation compatible mail classification and to pass the savings on to mailers. If productivity does not dramatically increase as a result of mailers' efforts to prepare automation compatible mail, the prospects for survival of the Postal Service as we now know it are bleak.

In the face of the new technology and alternate media, rising postal rates will force all mailers to curtail their use of the mail as they attempt to cut costs. That is happening. The PMG has stated clearly in recent months that the Postal Service is losing its market share in the communications of our great nation as a result of new technology and old competitors. Even worse, postal mail volumes for the past few years have grown significantly less than the growth of the overall American economy and less than historic mail volume growth. What happens when volume is stagnant or declining? The costs of the universal delivery network fall on fewer and fewer pieces of mail—which, in turn, increases the costs of mail delivery—which increases rates—which causes further reduction in mail volume. Moreover, the first mail volumes to leave the system are usually the least expensive for the Postal Service to process. For example, the loss of third-class volume would eliminate or reduce its $3.36 billion contribution to overhead costs, which would require other users of the Postal Service to pay the lost $3.36 billion. Rates simply go higher and higher.

The 19 million Americans whose employment depends on direct marketing cannot allow this downward volume spiral and upward rate spiral to continue. New communications media in the information age should complement existing media, not

replace it. For business mailers, we see the new media as adding to the marketing mix—not necessarily supplanting existing media. This, of course, assumes that rates and service are competitive. Mail volume should be growing at a robust rate. The Postal Service must control its costs!

Moreover, consumers—our customers—would be adversely affected by spiraling postage rates. Research indicates that consumers enjoy receiving mail and information on products and services available to them. The growth of our industry is based on consumer acceptance of direct marketing. In fact, over 52 percent of Americans shopped at home last year.

How can this happen? After months of discussion, arguments, and more discussion among our members, DMA believes that the best past path to achieve postal cost reductions in the long run is through the discipline of competition. Competition—and the potential for failure—will give all those involved in the Postal Service a sense of urgency to control costs and become more competitive in the communications market. However, immediately moving into a truly competitive environment for the U.S. Mail would wreak havoc on every industry dependent upon the Postal Service. Neither the Postal Service nor its present and potential competitors are ready to switch to an open market for a business delivering over 180 billion pieces of mail with $55 billion in annual revenues. Direct marketers and the Americans employed to support them could not withstand even a one-month disruption in the universal hard-copy delivery system. A breakdown in mail delivery would cause significant harm to the Nation's economy. Any move toward competition must be phased in, allowing the Postal Service, its employees, the mailers, and competitors adequate opportunity to adjust and prepare. Senator Stevens, DMA applauds your request to each witness at these hearings for suggestions of postal reforms which could be enacted this year. Moving directly to competition is not one of them. We believe there are other steps that must be taken first.

DMA believes that if the Postal Service were given more flexibility over rates and classification, it would have more tools to enable it to control costs and improve its financial viability. Attached to my testimony is draft legislation to give the Service more flexibility. Many of the provisions in the attached draft were crafted in discussions among mailers, postal employee organizations, and the Postal Service 4 years ago. As you can see, this subject has been around for many years. We have updated the proposals and believe they represent an appropriate basis for discussion of the first steps in postal reform legislation.

Briefly the draft legislation would:

1. Allow the Postal Service to adjust postal rates without a rate proceeding at the Postal Rate Commission, if USPS costs are below the rate of wage inflation; all rates would be changed by the same proportion; rate increases would be restricted to 75 percent of the Employee Compensation Index (ECI); rates could be adjusted no more than once every 12 months; and rates could not be adjusted under this section more than 5 years after the last Postal Rate Commission recommended general rate change. Thus, an omnibus rate case allowing for a full hearing before the Postal Rate Commission would be required periodically. This maintains the role of the Postal Rate Commission to insure that monopoly classes would not cross-subsidize other Postal Service products, and allow for corrections of any rate anomalies that might have crept into the rate structure because of changing costs generated by each class of mail.
2. Allow the entire Board of Governors, not just the nine presidentially appointed Governors, to vote on all Postal Rate Commission recommendations. Currently, only the nine presidentially appointed governors can vote on the final disposition of Postal Rate Commission recommendations. The full Board, however, also consists of the Postmaster General and the Deputy Postmaster General who are selected by the Governors. We believe that they, too, should have a vote in this critical area of ratemaking.
3. Provide that a three-fourths majority of the Board of Governors may modify a further recommended decision of the Postal Rate Commission rather than the unanimous vote now required.
4. Allow the Postal Service to test experimental service offerings without seeking a Postal Rate Commission recommendation, provided the experiment is limited in both scope and duration.
5. Allow the Postal Service to change mail classifications *which do not change rates* through notice and comment rulemaking;
6. Allow the Postal Service to make limited changes in the nature of postal services through notice and comment rulemaking;

7. Provide subpoena power to the Postal Rate Commission for Postal Service documents and data specifically related to rate and mail classification case issues to help eliminate any delays caused by the failure of the Postal Service to provide the Commission the information it needs for its deliberations; and
8. Impose a deadline on Postal Rate Commission reconsideration of any recommended decision returned by the Board of Governors.

The draft legislation also provides for increased compensation for the Governors similar to the provisions sponsored by Senator Stevens earlier this Congress. We would suggest that these salaries be adjusted from time-to-time to reflect inflation. The draft also allows for bonuses for senior postal management that could exceed the statutory limit for compensation of postal officials. These two provisions are designed to improve the ability of the Postal Service to attract and retain qualified managers and Governors. There are also provisions granting the Postal Service greater freedom to handle its own finances and investments, freeing the Postal Service from restrictions on certain transportation contracts, and granting the Postal Service increased freedom over international mail arrangements.

This draft legislation grants the Postal Service much of the freedom it has been requesting over the past 5 years. It represents a first step in postal reform. How well the Postal Service performs with its new freedom will dictate both the content and the timing of the next step in the reform process. DMA urges you to give postal management more freedom and to hold them accountable for the results of their actions under their new freedom.

Again it has been a privilege to be asked to testify today, and I am ready to answer any questions you may have.

Thank you.

ATTACHMENT TO TESTIMONY OF JONAH GITLITZ, PRESIDENT AND CEO, DIRECT MARKETING ASSOCIATION

SECTION BY SECTION ANALYSIS

SECTION 1. SHORT TITLE.

The Postal Service Modernization Act of 1996.

SECTION 2. TABLE OF TITLES.

Title I. Employment and compensation.
Title II. Postal rates and services.
Title III. Financial activities.
Title IV. Transportation of mail.
Title V. International postal services.

TITLE I—EMPLOYMENT AND COMPENSATION

SECTION 101. SHORT TITLE.

The Postal Employment and Compensation Flexibility Act.

SECTION 102. COMPENSATION OF GOVERNORS OF THE POSTAL SERVICE.

Subsection (a) of this section amends 39 U.S.C. § 202(a) to raise the annual salary of the Governors of the Postal Service from $10,000 to $30,000, and to increase their fee per meeting from $300 to $900, and to index the annual and daily compensation in accordance with increases in Level I of the Executive Schedule.

Subsection (b) of this section further amends 39 U.S.C. § 202(a) to direct the Postal Service in fiscal year 1997, and every five fiscal years thereafter, to transmit to the appropriate legislative committees of the House and Senate its recommendations for adjustment in the Governors' compensation.

SECTION 103. EMPLOYMENT POLICY REGARDING COMPENSATION.

This section amends 39 U.S.C. § 1003(a) to provide that the level I Executive Schedule pay limit will apply specifically to the "salary" paid to an individual by the Postal Service, thus allowing additional compensation to an individual in the form of bonuses or awards, for example, to exceed that limit. Any such payment to an individual at or above the level of Assistant Postmaster General will require approval by a majority of the Governors of the Postal Service in office.

TITLE II—POSTAL RATES AND SERVICES

SECTION 201. SHORT TITLE.

The Postal Rate and Service Flexibility Act.

SECTION 202. RATEMAKING FLEXIBILITY FOR BOARD OF GOVERNORS.

Subsection (a) of this section amends 39 U.S.C. § 3624, adding new subsection (e) to establish time limits for the Postal Rate Commission to reconsider a recommended decision on postal rates or changes in the mail classification schedule which is returned to the Commission by the Board of Governors. The Commission will have 90 days after the decision was returned to transmit its further recommended decision to the Board.

Subsection (b) of this section revises 39 U.S.C. § 3625 to enhance the flexibility of the governing board of the Postal Service to respond to a recommended decision from the Postal Rate Commission.

Section 3625(a) provides that the full Board of Governors (including the Postmaster General and Deputy Postmaster General) will exercise the options to approve, allow under protest, reject, or modify a recommended decision of the Postal Rate Commission.

Section 3625(b) provides that the Board may approve a recommended decision and order it placed in effect.

Section 3625(c) provides that the Board may allow a recommended decision to take effect under protest and (1) seek judicial review under 39 U.S.C. § 3628, or (2) return the recommended decision to the Commission for reconsideration and a further recommended decision.

Section 3625(d) provides that the Board may reject a recommended decision, and (1) take no further action, or (2) return the recommended decision to the Commission for reconsideration and a further recommended decision.

Section 3625(e) provides that when a further recommended decision is received from the Commission, the Board may modify that further recommended decision with the written concurrence of three-quarters of the Board in office. Those members must expressly find that (1) the modification is in accord with the record and the policies of subchapter II of chapter 36 of title 39, and (2) the rates recommended by the Commission are not adequate to provide sufficient revenues.

Section 3625(f) requires that the decision of the Board to approve, allow under protest reject or modify a recommended decision shall include an estimate of anticipated revenue and a statement of explanation and justification. The time for making the decision and record available for sale by the Public Printer is extended to 15 days following the Board of Governors' decision.

Section 3625(g) provides that the Board will determine the date on which rate or classification changes go into effect.

Subsection (c) of this section amends 39 U.S.C. § 3641 to allow the establishment of temporary changes in rates of postage, fees for postal services and classifications of mail when the Commission does not transmit a further recommended decision to the Board in accordance with the time limits established in 39 U.S.C. § 3624(e).

Subsection (d) of this section makes conforming amendments in 39 U.S.C. §§ 3621, 3623, 3624, 3628, 3641, and 3684 to reflect that the full Board of Governors, and not the Governors acting in their separate capacity, will act upon rate and classification changes.

Subsection (e) of this section makes a conforming amendment to the table of sections.

SECTION 203. INDEXED ADJUSTMENT OF POSTAL RATES.

Subsection (a) of this section enacts new 39 U.S.C. § 3629 to permit the annual indexed adjustment of postal rates and fees.

Section 3629(a) provides that the Board of Governors may approve an indexed adjustment in postal rates and fees no more often than once in any fiscal year. Any such adjustment will produce as nearly as practicable the same percentage of change in each rate element in the Postal Service rate schedule. The adjustment will not apply to rates or fees, such as those for international mail, not subject to 39 U.S.C. §§ 3621 through 3628.

Section 3629(b) provides that the maximum average percentage of change in any indexed adjustment shall not exceed three-quarters of the percentage of change in the Employment Cost Index (ECI) since the date of the last indexed adjustment, or omnibus change in postal rates under 39 U.S.C. § 3625, whichever is more recent.

Section 3629(c) directs the Postal Service to maintain and publish at least quarterly its own Index of Unit Postal Costs (IUPC), which will record the percentage of change in total resource prices paid by the Postal Service (excluding costs not or-

dinarily experienced by businesses in the general economy), modified by any changes in postal productivity and adjusted to take into account changes in Postal Service operations caused by factors such as changes in total volume, volume mix and number of addresses served. The IUPC shall be computed by the Postal Service in accordance with specifications promulgated by the Postal Rate Commission through notice-and-comment rulemaking.

Section 3629(d) provides that if the increase in the IUPC over at least a year is less than the increase in the ECI over the same period, the Postal Service may adjust postal rates and fees by an average percentage no greater than the maximum percentage defined in section 3629(b).

Section 3629(e) requires the Postal Service to transmit a request for certification of any indexed adjustment to the Postal Rate Commission. The request must include supporting information concerning the changes in the IUPC and ECI, information verified by an independent party regarding the level of postal services provided during the period covered by the request, and a proposed effective date no less than 120 days after the request.

Section 3629(f) directs the Commission to consider the request, providing at least 30 days for public comment, and transmit its response to the Board of Governors within 90 days. The Commission shall certify the adjustment if it determines that the supporting information is accurate, that there has not been a significant decline in the level of postal services during the relevant period, and that the proposed adjustment otherwise satisfies the requirements of section 3629.

Section 3629(g) provides that if the Commission is unable to certify the adjustment, it shall transmit its written objections in its response to the Board. The Board may transmit a further amended request for certification to the Commission, which shall transmit its further response within 30 days.

Section 3629(h) provides that if the Commission fails to transmit its response or further response to the Board within the time provided, or if the Board determines that the Commission has unreasonably withheld certification, three-quarters of the Board in office may order the adjustment placed into effect.

Section 3629(i) provides that the Postal Service may not propose an indexed adjustment at any time later than 60 months following the most recent omnibus change in postal rates under 39 U.S.C. § 3625.

Subsection (b) of this section makes a conforming amendment to the table of sections.

SECTION 204. ESTABLISHMENT OF NEW SUBCHAPTER.

Subsection (a) of this section redesignates former subchapters III, IV, and V of chapter 36 of title 39, and inserts a new subchapter III, dealing exclusively with flexible rates and services.

Subsection (b) of this section makes conforming amendments to 39 U.S.C. §§ 3681 and 3682 to include new subchapter III in the provisions dealing with reimbursement for past postage payments and the establishment of size and weight limits.

Subsection (c) of this section makes a conforming amendment to the table of sections.

SECTION 205. MARKET TESTS OF EXPERIMENTAL SERVICES.

Subsection (a) of this section enacts new 39 U.S.C. § 3632 to permit the Postal Service to conduct market tests of experimental postal services.

Section 3632(a) allows the Postal Service to conduct market tests of experimental postal services, using such variable factors as the Postal Service deems appropriate. No such market test may last longer than two years, or be designed to involve more than $100,000,000 of postal revenue, or two percent of the total revenue from a particular type of mail or service, whichever is greater.

Section 3632(b) requires the Postal Service to request the Postal Rate Commission to certify a proposed test at least 60 days in advance, providing reasonable information about the nature of the test, its duration, and its expected impact on postal revenues.

Section 3632(c) requires the Commission to transmit its response to the Postal Service within 30 days. The Commission may certify that the proposed test satisfies the time and revenue requirements of section 3632(a), or may request the Postal Service to provide reasonably necessary additional information. The Postal Service will postpone the date of the proposed test to allow the Commission 30 days to consider the information provided. If the Commission, after 30 days, does not certify the proposed test, the Postal Service will take no action to conduct the test, except by a resolution of three-quarters of the Board of Governors in office.

Section 3632(d) provides that an interested party who believes that a market test does not conform to the policies of title 39 may lodge a complaint with the Commis-

sion under 39 U.S.C. § 3662. The Commission may expedite its consideration of the complaint, as a matter not covered by subchapter II of chapter 36, but may not suspend the progress of the test.

Subsection (b) of this section makes a conforming amendment to the table of sections.

SECTION 206. EXPEDITED MAIL CLASSIFICATION CHANGES.

Subsection (a) of this section enacts new 39 U.S.C. § 3634 to authorize the Postal Service to make limited changes in the mail classification schedule through rulemaking procedures.

Section 3634(a) allows the Postal Service to modify the mail classification schedule established under 39 U.S.C. § 3623. Any such modification shall primarily concern a single class or subclass of mail or type of service, shall not establish a new rate element for any class of mail or type of service, and must be approved by three-quarters of the Board of Governors in office.

Section 3634(b) requires the Postal Service to publish a notice of any proposed classification change in the Federal Register, allowing at least 30 days for written comment.

Section 3634(c) requires the Postal Service, after considering written comments, to determine whether oral comment is necessary or appropriate. If oral comment is required, the Postal Service will publish in the Federal Register a schedule of hearings on the proposed change, and conduct such hearings in such manner, times, and locations as it determines will facilitate public participation.

Section 3634(d) requires the Postal Service, after considering the views expressed, to publish in the Federal Register a final notice explaining its decision to adopt, modify and adopt, or withdraw the proposed change. If a proposed or modified change is adopted, the final notice will give at least 30 days' notice of the effective date.

Section 3634(e) provides that before the effective date, an interested party who believes that a classification change under this section does not conform to the policies of title 39 may lodge a complaint with the Commission under 39 U.S.C. § 3662. The Commission may expedite its consideration of the complaint, as a matter not covered by subchapter II of chapter 36, but may not suspend the effectiveness of the classification change.

Subsection (b) of this section makes a conforming amendment to the table of sections.

SECTION 207. EXPEDITED SERVICE CHANGES.

Subsection (a) of this section enacts new 39 U.S.C. § 3635 to authorize the Postal Service to make limited changes in the nature of postal services through rulemaking procedures.

Section 3635(a) allows the Postal Service to make changes in the nature of postal services which will generally affect service on a nationwide or substantially nationwide basis. Any such change shall not cause any substantial reduction in the overall level of service provided to postal customers, and must be approved by three-quarters of the Board of Governors in office.

Section 3635(b) requires the Postal Service to publish a notice of any proposed service change in the Federal Register, allowing at least 90 days for written comment. The notice will also contain a schedule of public hearings on the proposed change, which the Postal Service will conduct in such manner, times, and locations as it determines will facilitate public participation.

Section 3635(c) requires the Postal Service, after considering the views expressed, to publish in the Federal Register a final notice explaining its decision to adopt, modify and adopt, or withdraw the proposed change. If a proposed or modified change is adopted, the final notice will give at least 30 days' notice of the effective date.

Section 3634(e) provides that before the effective date, an interested party who believes that a service change under this section does not conform to the policies of title 39 may lodge a complaint with the Commission under 39 U.S.C. § 3662. The Commission may expedite its consideration of the complaint, as a matter not covered by subchapter II of chapter 36, but may not suspend the effectiveness of the service change.

Subsection (b) of this section makes a conforming amendment to the table of sections.

SECTION 208. SUBPOENA AUTHORITY.

Subsection (a) of this section enacts new 39 U.S.C. § 3630 to give the Commission subpoena authority to compel the production of Postal Service documents relevant to a proceeding before it.

Section 3630(a) authorizes the Commission acting by majority vote to compel, through issuance of a subpoena addressed to the Postmaster General or other appropriate official of the Postal Service, the production by the Postal Service of any books, papers, correspondence, memoranda, studies, data or other records within the possession or control of the Postal Service which the Commission deems relevant or material to such proceeding. Such production of any such records may be required from any place in the United States or any State at the offices of the Commission.

Section 3630(b) provides that this subpoena power not apply to (i) any person other than the United States Postal Service and officers thereof, or (ii) trade secrets and commercial or financial information which are (x) in the possession of the Postal Service and obtained from a person other than the Postal Service and (y) privileged or confidential.

Section 3630(c) provides that in case of refusal to obey a subpoena issued pursuant to this section, the Commission may invoke the aid of the United States District Court for the District of Columbia or any court of the United States in requiring the production of books, papers, correspondence, memoranda, studies, data and other records. Such court may issue an order requiring the Postmaster General or other appropriate official of the Postal Service to appear before the Commission there to produce records, if so ordered, relevant to any matter at issue in the proceeding in question; and any failure to obey such order of the court may be punished by such court as a contempt thereof. All process in any such case may be served in the judicial district whereof such person is an inhabitant or wherever he may be found. Any person who shall, without just cause, fail or refuse to attend or to answer any lawful inquiry or to produce books, papers, correspondence, memoranda, studies, data and other records, if in his power so to do, in obedience to the subpoena of the Commission, shall be guilty of a misdemeanor and, upon conviction, shall be subject to a fine of not more than $1,000 or to imprisonment for a term of not more than one year, or both.

Section (b) of this section makes a conforming amendment to the table of sections.

SECTION 209. EFFECTIVE DATE.

This section makes this title effective upon enactment.

TITLE III—FINANCIAL ACTIVITIES

SECTION 301. SHORT TITLE.

The Postal Service Fiscal Administration Act.

SECTION 302. REDIRECTION OF POSTAL SERVICE BORROWING, DEPOSITS, AND INVESTMENTS TO PRIVATE MARKETS.

Subsection (a) of this section amends 39 U.S.C. §§2005 and 2006 to repeal the authority of the Secretary of the Treasury to preempt an issue of Postal Service obligations.

Subsection (a)(1) amends 39 U.S.C. §2005(d) to make Postal Service obligations "exempted securities," within the meaning of section 3(a)(2) of the Securities Act of 1933, section 3(a)(12) of the Securities Exchange Act of 1934, and section 304(a)(4) of the Trust Indenture Act of 1939, issued by an instrumentality of the Government of the United States.

Subsection (a)(2) revises 39 U.S.C. §2006(a) to require the Postal Service only to consult with the Secretary of the Treasury as to the timing and terms of sale of an issue of obligations under 39 U.S.C. §2005, thus removing the authority of the Secretary to preempt the issue by purchasing the obligations.

Subsection (b) of this section amends 39 U.S.C. §2003 to repeal the control of the Treasury over Postal Service deposits and investments.

Subsection (b)(1) amends 39 U.S.C. §2003 (a) and (b) to repeal the requirement that the Postal Service Fund be maintained in the Treasury of the United States, and amends 39 U.S.C. §2003(d) to repeal the requirement that the Secretary of the Treasury approve depositories for moneys of the Postal Service Fund.

Subsection (b)(2) amends 39 U.S.C. §2003(c) to repeal the requirement that the Secretary of the Treasury approve the investment of moneys of the Postal Service Fund in excess of current needs.

SECTION 303. EFFECTIVE DATE.

This section makes this title effective on such date, no later than one year after enactment as the Board of Governors shall prescribe.

TITLE IV—TRANSPORTATION OF MAIL

SECTION 401. SHORT TITLE.

The Mail Transportation Flexibility Act.

SECTION 402. DURATION OF TRANSPORTATION CONTRACTS.

Subsection (a) of this section amends 39 U.S.C. § 5005(b)(1) to increase the time limit on contracts for the surface and water transportation of mail from 4 to 10 years, and from 6 to 12 years where special conditions apply or special equipment is required.

Subsection (b) of this section amends 39 U.S.C. § 5212 to increase the time limit on special contracts for the surface transportation of mail from 4 to 10 years.

Subsection (c) of this section amends 39 U.S.C. § 5402(c) to increase the time limit on contracts for the transportation of mail by air taxi from 4 to 10 years.

SECTION 403. WEIGHT AND COMPOSITION RESTRICTIONS AND DEPARTMENT OF TRANSPORTATION APPROVAL REQUIREMENTS REMOVED.

This section amends 39 U.S.C. § 5402(a) to repeal the 750-pound minimum weight restriction and the five percent maximum letter weight limit on contracts for the transportation of mail by certificated air carriers in foreign air transportation. The option of the Secretary of Transportation to disapprove such contracts is repealed and replaced by the requirement that such contracts be filed with the Secretary 15 days in advance of their effective date, to assure conformity with 39 U.S.C. § 5005(b)(3).

SECTION 404. AUTHORITY TO CONTRACT FOR FOREIGN TRANSPORTATION AND SUPPORT SERVICES.

This section amends 39 U.S.C. § 5005, adding new subsection (d) to authorize the Postal Service to contract for the air or surface transportation of mail within and between foreign countries, and to contract for the acquisition and operation of air and surface terminals and hubs, and ground handling services, in support of such transportation.

SECTION 405. EFFECTIVE DATE.

This section makes this title effective upon enactment.

TITLE V—INTERNATIONAL POSTAL SERVICES

SECTION 501. SHORT TITLE.

The International Service Flexibility Act.

SECTION 502. AUTHORIZATION OF INTERNATIONAL POSTAL ARRANGEMENTS.

Subsection (a) of this section enacts new 39 U.S.C. § 414 to clarify the authority of the Postal Service to enter into a broad array of international service arrangements.

Section 414(a) authorizes the Postal Service to provide such international services as it determines necessary to meet the needs of the people of the United States.

Section 414(b) authorizes the Postal Service to take a wide variety of actions to provide international services, including but not limited to: concluding postal treaties, concluding money order agreements, entering into agreements with foreign postal administrations and entities in which they have an interest, establishing postal agencies in other countries, forming joint ventures or partnerships, creating separate legal entities, and acquiring interests in separate legal entities. This grants the Postal Service greater flexibility in dealing with foreign postal administrations and providing international postal services, particularly with respect to the use of cooperatives to support the exchange of international mail, and arrangements such as the impending joint venture of five postal administrations and TNT Ltd. to provide express courier services.

Section 414(c) provides that separate legal entities in which the Postal Service has or acquires an interest shall be subject to the laws applicable to firms in the private sector of the economy, and that provisions specifically applicable to the Postal Service shall not apply to such separate legal entities unless such provisions are generally applicable to firms in the private sector of the economy. This conforms to the practice of other nations, which treat separate legal entities such as those contemplated in section 414(b) as private companies. This avoids conflicts by making the treatment of such legal entities under United States law consistent with their treatment under foreign law.

Subsection (b) of this section further amends 39 U.S.C. § 2003 by adding a new subsection (h) to clarify that the obligation of funds by the Postal Service in connection with the provision of services is not deemed an investment of funds "in excess of current needs" within the terms of 39 U.S.C. § 2003(c). This ensures that Postal Service decisions to participate in joint ventures with other postal administrations or to acquire interests in separate legal entities in connection with providing international services would not be subject to approval by the Department of the Treasury, which has no responsibility for postal services or experience in postal operations.

Subsection (c) of this section makes a conforming amendment to 39 U.S.C. § 403(a).

Subsection (d) of this section makes a conforming amendment to the table of sections.

SECTION 503. EFFECTIVE DATE.

This section makes this title effective upon enactment.

A BILL

To amend title 39, United States Code, to enhance the employment and compensation flexibility of the Postal Service, to enable the Postal Service to make timely changes in postal rates and postal services, to redirect the financial activities of the Postal Service to private markets, to mitigate restrictions on the transportation of mail matter, to improve international postal arrangements, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled.

SEC. 1. SHORT TITLE.

This Act may be cited as the "Postal Service Modernization Act."

SEC. 2. TABLE OF TITLES.

Title I. Employment and compensation.
Title II. Postal rates and services.
Title III. Financial activities.
Title IV. Transportation of Mail.
Title V. International postal services.

TITLE I—EMPLOYMENT AND COMPENSATION (DELETED)

SEC. 101. SHORT TITLE.

This title may be cited as the "Postal Employment and Compensation Flexibility Act".

SEC. 102. COMPENSATION OF GOVERNORS OF THE POSTAL SERVICE.

(a) INCREASE IN COMPENSATION OF GOVERNORS.—Section 202(a) of title 39, United States Code, is amended by striking "$10,000 a year" and inserting in lieu thereof "$30,000 a year", by striking "$300 a day" and inserting in lieu thereof "$900 a day," and by inserting the following sentence at the end of Section 202(a): "The annual and daily compensation for the Governors, described above, shall be adjusted in the same proportion as the adjustments for level 1 of the Executive Schedule pursuant to section 5318, title 5, United States Code.".

(b) PERIODIC RECOMMENDATIONS CONCERNING COMPENSATION.—Section 202(a) of title 39, United States Code, is further amended by adding at the end thereof the following: "During fiscal year 1997, and every fifth fiscal year thereafter, the Postal Service shall transmit to the postal legislative committees of the Senate and the House of Representatives its recommendations for adjustment of the compensation provided to the Governors under this subsection.".

SEC. 103. EMPLOYMENT POLICY REGARDING COMPENSATION.

Section 1003(a) of title 39, United States Code, is amended by striking "paid compensation at a rate", and inserting in lieu thereof "paid a salary", and by adding at the end thereof the following: "Any payment to an individual employed by the Postal Service at or above the level of Assistant Postmaster General which would result in the payment of compensation to that individual in an amount in excess of the rate for level I of the Executive Schedule must be approved by a favorable vote of the majority of the Governors of the Postal Service in office.".

TITLE II—POSTAL RATES AND SERVICES

SEC. 201. SHORT TITLE.

This title may be cited as the "Postal Rate and Service Flexibility Act."

SEC. 202. RATEMAKING FLEXIBILITY FOR BOARD OF GOVERNORS.

(a) TIME FOR FURTHER RECOMMENDED DECISION.—Section 3624 of title 39, United States Code, is amended by adding at the end thereof the following:

"(e) The Commission shall promptly reconsider a recommended decision returned to it under section 3625 (c) or (d) of this title, and shall transmit a further recommended decision to the Board of Governors no later than 90 days after the original recommended decision was returned."

(b) MODIFICATION AUTHORITY OF BOARD OF GOVERNORS.—Section 3625 of title 39, United States Code, is revised to read as follows:

"§ 3625. Action of the Board of Governors

"(a) Upon receiving a recommended decision from the Postal Rate Commission, the Board of Governors may approve, allow under protest, reject, or modify that decision in accordance with the provisions of this section.

"(b) The Board may approve the recommended decision and order the decision placed in effect.

"(c) The Board may, under protest, allow a recommended decision of the Commission to take effect and (1) seek judicial review thereof under section 3628 of this title, or (2) return the recommended decision to the Commission for reconsideration and a further recommended decision, which shall be acted upon under this section and subject to review in accordance with section 3628 of this title.

"(d) The Board may reject the recommended decision of the Commission and (1) take no further action, or (2) return the recommended decision to the Commission for reconsideration and a further recommended decision, which shall be acted upon under this section and subject to review in accordance with section 3628 of this title.

"(e) Upon receiving a further recommended decision from the Commission under section 3624(e) of this title, with the written concurrence of three-quarters of the members of the Board of Governors in office, the Board may modify any such further recommended decision of the Commission under this subsection if those members of the Board expressly find that (1) such modification is in accord with the record and the policies of this subchapter, and (2) the rates recommended by the Commission are not adequate to provide sufficient total revenues so that total estimated income and appropriations will equal as nearly as practicable estimated total costs.

"(f) The decision of the Board to approve, allow under protest, reject, or modify a recommended decision of the Commission shall be in writing and shall include an estimate of anticipated revenue and a statement of explanation and justification. The decision, the record of the Commission's hearings, and the Commission's recommended decision shall be made generally available at the time the decision is issued and shall be printed and made available for sale by the Public Printer within 15 days following the day the decision is issued.

"(g) The Board shall determine the date on which the new rates, fees, and changes in the mail classification schedule under this subchapter shall become effective."

(c) FAILURE TO COMPLY WITH TIME LIMITS.—Section 3641 of title 39, United States Code, is amended:

(1) in subsection (a) by inserting "or a further recommended decision in accordance with section 3624(e) of this title," immediately following "section 3624(c) of this title,";

(2) in subsection (d) by striking "it recommended decision" and inserting in lieu thereof "its recommended decision," and by inserting "or its further recommended decision under section 3624(e) of this title," immediately following "section 3624(d) of this title,"; and

(3) in subsection (e) by inserting "under section 3625 (c) or (d) of this title" immediately following "Postal Service has resubmitted."

(d) CONFORMING AMENDMENTS.—Sections 3621, 3623(b), 3624(c)(1) and (d), 3628, 3641 (a), (d), and (e) (as amended by this section), and 3684 of title 39, United States Code, are amended by inserting "Board of" immediately before "Governors" each time that word appears.

(e) TABLE OF SECTIONS.—The item relating to section 3625 in the table of sections for chapter 36 of title 39, United States Code, is amended to read as follows:

"3625. Action of the Board of Governors."

SEC. 203. INDEXED ADJUSTMENT OF POSTAL RATES.

(a) INDEXED ADJUSTMENT OF RATES.—Subchapter II of chapter 36 of title 39 United States Code, is amended by inserting after section 3628 the following new section:

"§ 3629. Indexed adjustment of postal rates

"(a) Notwithstanding any other provision of this subchapter, the Postal Service may, to the extent it deems appropriate, adjust rates of postage and fees for postal services no more frequently than once in any fiscal year in accordance with the indexing procedures established in this section. Any such indexed adjustment in rates and fees shall produce as nearly as practicable the same percentage of change in the rates for each rate element in the Postal Service rate schedule, and shall require a resolution approved by an absolute majority of the members of the Board of Governors in office. The provisions of this section shall not apply to any change in a rate or fee not subject to the provisions of sections 3621 through 3628 of this title.

"(b) The maximum average percentage of change in any indexed adjustment in rates and fees under this section shall not exceed three-quarters of the percentage of change in the Employment Cost Index (ECI) published by the Department of Labor, since the date of the most recent indexed rate adjustment under this section, or the most recent omnibus change in postal rates under section 3625 of this title, whichever is more recent.

"(c) The Postal Service shall maintain and publish no less often than quarterly an Index of Unit Postal Costs (IUPC) which shall record the percentage of change in the total resource prices paid by the Postal Service, including (without limitation) operating expenses (including the costs of wages, benefits, transportation, utilities, equipment, and supplies), depreciation in economic value of facilities and equipment and the equivalent commercial cost of borrowing, but excluding any retroactive or otherwise exceptional costs imposed on the Postal Service by legislation or otherwise which are not typical of costs ordinarily experienced by businesses in the general economy, modified by any changes in postal productivity measured and adjusted to take into account changes in Postal Service operations caused by factors such as changes in total volume, volume mix and number of addresses served. The IUPC shall be computed by the Postal Service in accordance with specifications promulgated by the Postal Rate Commission through notice-and-comment rulemaking.

"(d) If, in any period of not less than a year, an increase in the IUPC is less than an increase in the ECI, the Postal Service may in its discretion adjust the rates of postage and fees for postal services then currently in effect by an average percentage which does not exceed the maximum percentage defined in subsection (b) of this section.

"(e) When the Postal Service proposes to adjust rates and fees in accordance with subsection (d) of this section, it shall transmit a request for certification of the proposed adjustments to the Postal Rate Commission. Such request shall include the resolution of the Board of Governors approving the adjustments, supporting information concerning changes in the IUPC and the ECI during the relevant period, information verified by an independent party outside the Postal Service regarding the level of postal services provided during the relevant period, and a proposed effective date no less than 120 days after the date of such request.

"(f) The Commission shall consider the request, and shall by public notice provide an opportunity of no less than 30 days for interested parties and users of the mails to provide written comments regarding the proposed adjustments. The Commission shall transmit its response to the Board of Governors no later than 90 days after receiving any such request from the Postal Service, and shall certify that the adjustments may take effect on the proposed date if the Commission finds: (1) that the Postal Service has provided accurate information regarding changes in the IUPC and the ECI during the relevant period; (2) that there has not been a material decline in the level of postal services during the relevant period; and (3) that the proposed adjustments satisfy the requirements of subsections (a), (b), or (d) of this section.

"(g) if the Commission determines that it is unable to provide the certification required by subsection (f) of this section, it shall include a written statement of its objections in its response to the Board of Governors. The Board shall consider the Commission's objections, and may transmit a further amended request for certification to the Commission. The Commission shall consider any such further request, and shall transmit its further response to the Board no later than 30 days after receiving any such further request.

"(h) If the Commission does not transmit its response or its further response to the Board within the time established by subsection (f) or (g) of this section, or if the Board determines that the Commission has unreasonably withheld certification in any such response or further response, the Board may order the proposed adjustments placed into effect by a resolution approved by three-quarters of the members of the Board of Governors in office.

"(i) Notwithstanding any other provision of this section, the Postal Service shall not propose to adjust rates and fees under this section at any time later than 60 months following the date of the most recent omnibus change in postal rates under section 3625 of this title."

(b) TABLE OF SECTIONS.—The table of sections for chapter 36 of title 39, United States Code, is amended by inserting immediately after the item relating to section 3628 the following new item:

"3629. Indexed adjustment of postal rates."

SEC. 204. ESTABLISHMENT OF NEW SUBCHAPTER.

(a) NEW SUBCHAPTER ESTABLISHED CONCERNING FLEXIBLE RATES AND SERVICES.—Chapter 36 of title 39, United States Code, is amended by redesignating subchapters III, IV, and V as subchapters IV, V, and VI, respectively, and by inserting a new subchapter III, entitled "FLEXIBLE RATES AND SERVICES."

(b) CONFORMING AMENDMENTS.—Sections 3681 and 3682 of title 39, United States Code, are amended by inserting "or subchapter III" immediately after "subchapter II" each time those words appear.

(c) TABLE OF SECTIONS.—The table of sections for chapter 36 of title 39, United States Code, is amended by inserting before the item for subchapter IV, as redesignated by this Act, the following new subchapter heading:

"SUBCHAPTER III—FLEXIBLE RATES AND SERVICES."

SEC. 205. MARKET TESTS OF EXPERIMENTAL SERVICES.

(a) MARKET TESTS OF SERVICES AUTHORIZED.—Subchapter III of chapter 36 of title 39, United States Code, as established by this Act, is amended by inserting in its proper order the following new section:

"§ 3632. Experimental postal services

"(a) Notwithstanding any other provision of law, when it considers such action necessary or desirable, the Postal Service as authorized by the Board of Governors may conduct market tests of experimental postal services. Such a market test may include geographic or other variations in such factors as the Postal Service may deem appropriate, including but not limited to postal rates and fees, mail classification requirements, postal products and equipment, and the terms and conditions under which postal services are provided. No such market test may have a duration of more than two years, or be designed to implicate more than $100,000,000 of postal revenues, or two percent of the total revenue from a particular class, subclass, or rate category of mail, or type of service, whichever is greater.

"(b) When the Postal Service intends to conduct a market test of an experimental postal service, it shall transmit a written request to certify the proposed test no less than 60 days in advance to the Postal Rate Commission, including a description of the test and such information as may be reasonably required to show its anticipated duration and its estimated impact on postal revenues.

"(c) No more than 30 days after receiving a request to certify a proposed market test, the Commission shall transmit its written response to the Postal Service. The Commission may certify that the test, as described, appears to fall within the time and revenue limits prescribed in subsection (a) of this section, or request the Postal Service to provide such additional information as may be reasonably required for such a determination. In any instance where the Commission requests additional information, the Postal Service shall postpone the date of the proposed test to allow the Commission an additional 30 days to consider the information provided. If the Commission, after such time, does not certify that the proposed test appears to fall within the limits prescribed in subsection (a) of this section, the Postal Service shall take no action to conduct the test, except by a resolution approved by three-quarters of the members of the Board of Governors in office.

"(d) Any interested party who believes that a market test conducted by the Postal Service under this section does not conform to the policies of this title may lodge a complaint with the Postal Rate Commission in accordance with the provisions of section 3662 of this title. The Commission may expedite its consideration of such complaint in accordance with the provisions of that section, as a matter not covered by subchapter II of this chapter, but may not suspend the progress of the test."

(b) TABLE OF SECTIONS.—The table of sections for chapter 36 of title 39, United States Code, is amended by inserting in its proper order in subchapter III the following new item:

"3632. Experimental postal services."

SEC. 206. EXPEDITED MAIL CLASSIFICATION CHANGES.

(a) PROCEDURE FOR EXPEDITED CLASSIFICATION CHANGES.—Subchapter III of chapter 36 of title 39, United States Code, as established by this Act, is amended by inserting in its proper order the following new section:

"§ 3634. Expedited mail classification changes

"(a) Notwithstanding any other provision of law, the Postal Service may from time to time, as it deems appropriate, modify the mail classification schedule established under section 3623 of this title. Any such modification under this section shall be primarily concerned with a single class or subclass of mail or type of service, shall not establish a new rate element for any class of mail or type of service, and shall become effective only by a resolution approved by three-quarters of the members of the Board of Governors in office.

"(b) When the Postal Service determines that it would be appropriate to modify the currently existing mail classification schedule, it shall publish in the Federal Register a notice of the proposed change. Such notice shall include an explanation of the proposed change, and allow no less than 30 days for interested persons to submit written data, views, or arguments concerning the proposed change.

"(c) After the conclusion of the comment period, the Postal Service shall determine, after consideration of the relevant matter presented, whether it is necessary or appropriate to afford an opportunity for oral presentation regarding the proposed change. If the Postal Service determines that such an opportunity is required, it shall publish in the Federal Register a schedule of public hearings on the proposed change, and shall conduct such hearings in such manner and at such times and locations as it determines will facilitate public participation.

"(d) After consideration of the views expressed, the Postal Service shall publish in the Federal Register a final notice regarding the proposed change. The final notice shall contain an analysis of the written views and any oral comments received, and may adopt, modify and adopt, or withdraw the proposed change. If the proposed change or a modification of the proposed change is adopted, the final notice shall include the resolution of the Board of Governors approving the change, together with an effective date no less than 30 days after the date of publication.

"(e) Before the effective date, any interested party who believes that a classification change adopted by the Postal Service under this section does not conform to the policies of this title may lodge a complaint with the Postal Rate Commission in accordance with the provisions of section 3662 of this title. The Commission may expedite its consideration of such complaint in accordance with the provisions of that section, as a matter not covered by subchapter II of this chapter, but may not suspend the effectiveness of the classification change."

(b) TABLE OF SECTIONS.—The table of sections for chapter 36 of title 39, United States Code is amended by inserting in its proper order in subchapter III the following new item:

"3634. Expedited mail classification chances."

SEC. 207. EXPEDITED SERVICE CHANGES.

(a) PROCEDURE FOR EXPEDITED SERVICE CHANGES.—Subchapter III of chapter 36 of title 39, United States Code, as established by this Act, is amended by inserting in its proper order the following new section:

"§ 3635. Expedited service changes

"(a) Notwithstanding any other provision of law, the Postal Service may from time to time, as it deems appropriate, determine that there should be a change in the nature of postal services which will generally affect service on a nationwide or substantially nationwide basis. Any such change under this section shall not effect any substantial reduction in the overall level of service provided to postal customers, and shall become effective only by a resolution approved by three-quarters of the members of the Board of Governors in office.

"(b) When the Postal Service determines that it would be appropriate to change the nature of postal services in any respect which will generally affect service on a nationwide or substantially nationwide basis, it shall publish in the Federal Register a notice of the proposed change. Such notice shall include an explanation of the proposed change, and allow no less than 90 days for interested persons to submit written data, views or arguments concerning the proposed change. To afford an

opportunity for oral presentation regarding the proposed change, such notice shall also include a schedule of public hearings on the proposed change, to be conducted in such manner and at such times and locations as the Postal Service determines will facilitate public participation.

"(c) After consideration of the views expressed, the Postal Service shall publish in the Federal Register a final notice regarding the proposed change. The final notice shall contain an analysis of the written and oral comments received, and may adopt, modify and adopt, or withdraw the proposed change. If the proposed change or a modification of the proposed change is adopted, the final notice shall set forth the resolution of the Board of Governors approving the change, together with an effective date no less than 30 days after the date of publication.

"(d) Before the effective date, any interested party who believes that a service change adopted by the Postal Service under this section does not conform to the policies of this title may lodge a complaint with the Postal Rate Commission in accordance with the provisions of section 3662 of this title. The Commission may expedite its consideration of such complaint in accordance with the provisions of that section, as a matter not covered by subchapter II of this chapter, but may not suspend the effectiveness of the service change."

(b) CONFORMING AMENDMENT.—Section 3661(b) of title 39, United States Code is amended by striking "When" and inserting in lieu thereof "Except as provided in section 3635 of this title, when."

(c) TABLE OF SECTIONS.—The table of sections for chapter 36 of title 39, United States Code, is amended by inserting in its proper order in subchapter III the following new item:

"3635. Expedited service changes."

SECTION 208. SUBPOENA AUTHORITY.

(a) SUBPOENA AUTHORITY.—Subchapter II of chapter 36 of title 39, United States Code is amended by inserting after section 3629 the following new section:

"§ 3630. Subpoena authority.

"(a) For the purpose of any proceeding under this title, the Commission acting by majority vote is empowered to compel, through issuance of a subpoena addressed to the Postmaster General or other appropriate official of the Postal Service, the production by the Postal Service of any books, papers, correspondence, memoranda, studies, data or other records within the possession or control of the Postal Service which the Commission deems relevant or material to such proceeding. Such production of any such records may be required from any place in the United States or any State at the offices of the Commission.

"(b) The authority granted in this Section shall not apply to (i) any person other than the United States Postal Service and officers thereof, or (ii) trade secrets and commercial or financial information which are (x) in the possession of the Postal Service and obtained from a person other than the Postal Service and (y) privileged or confidential.

"(c) In case of refusal to obey a subpoena issued pursuant to this section, the Commission may invoke the aid of the United States District Court for the District of Columbia or any court of the United States in requiring the production of books, papers, correspondence, memoranda, studies, data and other records. Such court may issue an order requiring the Postmaster General or other appropriate official of the Postal Service to appear before the Commission there to produce records, if so ordered, relevant to any matter at issue in the proceeding in question; and any failure to obey such order of the court may be punished by such court as a contempt thereof. All process in any such case may be served in the judicial district whereof such person is an inhabitant or wherever he may be found. Any person who shall, without just cause, fail or refuse to attend or to answer any lawful inquiry or to produce books, papers, correspondence, memoranda, studies, data and other records, if in his power so to do, in obedience to the subpoena of the Commission, shall be guilty of a misdemeanor and, upon conviction, shall be subject to a fine of not more than $1,000 or to imprisonment for a term of not more than one year, or both."

(b) TABLE OF SECTIONS.—The table of sections for chapter 36 of title 39, United States Code, is amended by inserting immediately after the item relating to section 3629 the following new item:

"3630. Subpoena authority."

SEC. 209. EFFECTIVE DATE.

The provisions of this title shall take effect on the date of enactment of this Act.

TITLE III—FINANCIAL ACTIVITIES

SEC. 301. SHORT TITLE.

This title may be cited as the "Postal Service Fiscal Administration Act."

SEC. 302. REDIRECTION OF POSTAL SERVICE BORROWING, DEPOSITS, AND INVESTMENTS TO PRIVATE MARKETS.

(a) TREASURY PREEMPTION OF POSTAL SERVICE OBLIGATIONS REPEALED.——

(1) IN GENERAL.—Section 2005(d) of title 39, United States Code, is amended——

(A) in paragraph (1), by striking "and bearer or";

(B) in paragraph (4), by striking "and" after the semicolon;

(C) in paragraph (5), by striking the period and inserting "; and"; and

(D) by adding at the end the following:

"(6) be deemed to be 'exempted securities,' within the meaning of section 3(a)(2) of the Securities Act of 1933, section 3(a)(12) of the Securities Exchange Act of 1934 and section 304(a)(4) of the Trust Indenture Act of 1939, issued by an instrumentality of the Government of the United States."

(2) CONSULTATION WITH THE TREASURY.—Section 2006(a) of title 39, United States Code is amended to read as follows:

"(a) The Postal Service shall consult with the Secretary of the Treasury as to the timing and terms of sale of any obligations issued under section 2005 of this title.".

(b) TREASURY CONTROL OF POSTAL DEPOSITS AND INVESTMENTS REPEALED.——

(1) DEPOSITS.—Section 2003 of title 39, United States Code, is amended——

(A) in subsection (a), by striking "in the Treasury of the United States";

(B) in subsection (b), by striking "and" after the semicolon in paragraph (6), by striking the period at the end of paragraph (7) and inserting "; and", and by adding at the end the following:

"(8) the balance in the Postal Service Fund (as then established within the Treasury of the United States) immediately before the amendments made by the Postal Service Fiscal Administration Act take effect."; and

(C) in subsection (d)——

(i) by striking "With the approval of the Secretary of the Treasury, the" and inserting "The"; and

(ii) by striking "as the Postal Service and the Secretary may mutually agree" and inserting "as the Postal Service deems appropriate".

(2) INVESTMENTS.—Section 2003(c) of title 39, United States Code, is amended to read as follows:

"(c) If the Postal Service determines that the moneys of the Fund are in excess of current needs, it may invest such amounts as it deems advisable in obligations of, or obligations guaranteed by, the Government of the United States, or in such other securities as the Board of Governors shall consider appropriate.".

SEC. 303. EFFECTIVE DATE.

The amendments made by this title shall take effect on such date, no later than one year after the date of enactment of this Act, as the Board of Governors of the Postal Service shall prescribe.

TITLE IV—TRANSPORTATION OF MAIL

SEC. 401. SHORT TITLE.

This title may be cited as the "Mail Transportation Flexibility Act".

SEC. 402. DURATION OF TRANSPORTATION CONTRACTS.

(a) SURFACE AND WATER TRANSPORTATION.—Section 5005(b)(1) of title 39, United States Code, is amended by striking "4 years" and inserting in lieu thereof "10 years", and by striking "6 years" and inserting in lieu thereof "12 years".

(b) SPECIAL CONTRACTS.—Section 5212 of title 39, United States Code, is amended by striking the comma immediately following the word "advertising", and by striking "4 years" and inserting in lieu thereof "10 years".

(c) AIR TAXI TRANSPORTATION.—Section 5402(c) of title 39, United States Code, is amended by striking "4 years" and inserting in lieu thereof "10 years".

SEC. 403. WEIGHT AND COMPOSITION RESTRICTIONS AND DEPARTMENT OF TRANSPORTATION APPROVAL REQUIREMENTS REMOVED.

Section 5402(a) of title 39, United States Code, is amended by striking all after the first sentence thereof, and inserting in lieu thereof the following: "Any such contract shall be filed with the Secretary of Transportation not later than 15 days before its effective date.".

SEC. 404. AUTHORITY TO CONTRACT FOR FOREIGN TRANSPORTATION AND SUPPORT SERVICES.

Section 5005 of title 39, United States Code, is amended by inserting at the end thereof the following:

"(d) The Postal Service may contract for the transportation of United States Mail by air or surface within and between foreign countries, and may contract for the acquisition and operation of air and surface terminals and hubs, and for ground handling services, in support of such transportation.".

SEC. 405. EFFECTIVE DATE.

The provisions of this title shall take effect on the date of enactment of this Act.

TITLE V—INTERNATIONAL POSTAL SERVICES

SEC. 501. SHORT TITLE.

This title may be cited as the "International Service Flexibility Act".

SEC. 502. AUTHORIZATION OF INTERNATIONAL POSTAL ARRANGEMENTS.

(a) INTERNATIONAL SERVICE ARRANGEMENTS AUTHORIZED.—Chapter 4 of title 39, United States Code, is amended by inserting after section 413 the following new section:

"§ 414. International service arrangements

"(a) The Postal Service may provide such international services as it determines to be necessary to meet the needs of the people of the United States.

"(b) The Postal Service may make such arrangements and take such actions as it determines to be appropriate for providing international services, including, without limitation:

"(1) concluding postal treaties or conventions in accordance with section 407 of this title;

"(2) concluding money order agreements in accordance with section 408 of this title;

"(3) entering into agreements with foreign postal administrations and entities in which foreign postal administrations have an interest;

"(4) establishing postal agencies in other countries;

"(5) forming or joining joint ventures or partnerships;

"(6) creating separate legal entities; and

"(7) acquiring interests in separate legal entitles.

"(c) Except as otherwise provided by the Postal Service, legal entities in which the Postal Service has or acquires an interest shall be subject to the laws applicable to firms in the private sector of the economy, and no provision of title 39 or any other law applicable to the Postal Service shall apply to any legal entity in which the Postal Service has or acquires an interest unless that law is generally applicable to firms in the private sector of the economy.".

(b) INVESTMENT AUTHORITY CLARIFIED.—Section 2003 of title 39, United States Code, as amended by title III of this Act, is further amended by inserting at the end thereof the following:

"(h) The investment of funds by the Postal Service in connection with the provision of services is not an investment of funds 'in excess of current needs' within the terms of subsection (c) of this section.".

(c) CONFORMING AMENDMENT.—Section 403(a) of title 39, United States Code, is amended by striking "406 and 411" and inserting in lieu thereof "406, 411, 413, and 414".

(d) TABLE OF SECTIONS.—The table of sections for chapter 4 of title 39, United States Code, is amended by inserting immediately after the item relating to section 413 the following new item:

"414. International service arrangements.".

SEC. 503. EFFECTIVE DATE.

The provisions of this title shall take effect on the date of enactment of this Act.

TESTIMONY OF CHRIS McCORMICK, SENIOR VICE PRESIDENT, ADVERTISING AND DIRECT MARKETING, L.L.BEAN, INC.

Mr. McCORMICK. Mr. Chairman, my name is Christopher McCormick, and I'm the senior vice president for L.L.Bean, located in Freeport, Maine.

I would like to say how pleased I am to be here today to talk about a very important issue that is important to us.

As you might be aware, L.L.Bean is the largest catalog retailer in the sporting specialty field. We provide a wide range of products that allow our customers to pursue and enjoy their outdoor activities

L.L.Bean believes very strongly in providing our customers with fully- tested quality products and superior customer service. After all, it takes a great deal of trust for a customer in Fairbanks, for example, to place an order for a pair of hunting boots with a company located in Maine. In addition, if that customer in Fairbanks is not satisfied, it is very expensive for us to correct the mistake. Thus we learn very early on that there is no substitute for getting it right the first time, and that getting it right means satisfying the needs and expectations of our customers.

Meeting customers needs and expectations is L.L.Bean's fundamental business philosophy, and one that I know is shared today by the Postmaster General.

L.L.Bean interacts daily with its customers in four critical respects.

First, through our marketing efforts we attempt to make customers aware of our company and the full range of products we provide.

Second, our order processing facilities receive thousands of orders each day from our customers.

Third, we must fulfill the orders we receive and ensure that the products they purchase are delivered reliably and expeditiously.

And finally, we must provide our customers with a level of service that will earn their trust and encourage them to continue to buy our products.

The ways in which we interact with our customers involve technologies and processes that are constantly changing. Indeed, L.L.Bean is continuously searching for new and better ways to interact with our customers to ensure the shopping experience meets or exceeds their expectations. After all, our customers have many alternatives. This is only one way that we can ensure that they will continue to shop with us in the future.

Historically, virtually 100 percent of our interactions with our customers in each of the four areas that I have mentioned occurred through the U.S. Postal Service. In fact, when parcel post was introduced in 1912 by the U.S. Postal Service, a pair of L.L.Bean's hunting boots were in the first parcel to leave the Freeport Post Office.

Over time, however, in order to remain competitive in our business, we have responded to the demands of our customers by shifting various aspects of our operations to alternative technologies or competing vendors.

One significant shift away from the U.S. Postal Service occurred with the advent of 800 service 10 years ago. Our customers told us that they wanted faster service, direct access to our order processing facilities, and more information about our product line.

We responded with the now commonplace toll free number. Because this system better met the needs of our customers, it has grown continuously since its introduction. In fact, 10 years ago customer orders were split approximately 80 percent U.S. mail and 20 percent telephones. Today the split is reversed, and we expect that over the next 5 years our 800 service will account for 95 percent of our total orders.

The second shift away from the U.S. Postal Service has occurred more recently, as we moved our order fulfillment activities from the Postal Service to UPS and now Federal Express. As with 800 service, we have made this move because our customers demanded superior quality services at the best possible prices.

Interestingly, Federal Express has met our customers' needs through its superior use of information technology. The consequence to the Postal Service has been the loss of $45 million in revenue per year.

The third major shift has yet to occur, but when it does it will revolutionize our industry and our relationship with our customers. As a catalog marketer, L.L.Bean relies upon catalogs to provide our customers with information about the products we sell. This past year, for example, we mailed over 140 million catalogs to approximately 25 million households in this country. To do this, we rely on the Postal Service, just as we have since our first catalogs were mailed 84 years ago.

L.L.Bean, however, cannot remain stagnant as our customers change and impose new demands on us and our competitors. For example, this past year we experimented with limited broadcast advertising to reach customers in key market segments in an efficient and timely fashion.

We have also undertaken an aggressive program of exploring the use of electronic media, such as CD–ROM technology, and we are very interested in the potential of the Internet as a way to further communicate with our customers. In fact, this past October we established our own Website and are already having difficulty keeping up with the demands on the site. In January alone we had over 60,000 visitors to the site, approximately 15,000 of whom were international visitors, and about two-thirds of those were from Japan.

Since its inception, we have taken thousands of catalog requests and orders in just the first 6 months of operation. Perhaps as telling as the number of visitors we have had have been the suggestions they have left. These customers are telling us that they want to order merchandise on line, that they would like more information about our products, services, and outdoor activities, that this is a more convenient way for them to shop and they are very capable of using the technology.

An important business maxim for any retailer is to listen to your customers, and at L.L.Bean we steer by this principle. Many of our customers are now equipped and ready to enter the new age of communications, and we must be ready as well.

We cannot afford to ignore what these customers are telling us, nor can we afford to underestimate the urgency with which we must respond.

The telecommunications legislation you recently enacted is already being felt in our industry. AT&T's recent announcement of its intent to provide unlimited Internet access to its customers for $20 per month may have the same effect on our new generation of customers as its introduction of 800 service had on their parents a generation ago.

Whether we like it or not, the simple fact is that technology is rapidly becoming the driving force defining our interactions with our customers.

Imagine having the ability to obtain greater information about a product whenever you need it, download a video demonstrating how the product was made or to be used, and get recommendations on how use it, where to use it, such as national parks, campsites, or the best fishing locations. Providing value-added services like this is a new competitive arena and the last one in loses.

Our operations and experiences are not dissimilar from those from other firms in the direct marketing industry, and as such have profound implications for the U.S. Postal Service.

Postmaster General Runyon recognizes the competitive pressures the Postal Services faces. In a recent speech he stated, "Our competitors are beating us and beating us soundly in about every area of our business. Of our six major product areas, we are losing share in all but one."

The trends in our industries that have resulted in a loss of market share for the Postal Service are now threatening the remaining area in which it has retained its competitive advantage, standard mail services, specifically catalog distribution.

While the competitive threat to the Postal Service is real and growing, the consequences do not have to be a continuing erosion of market share or financial instability.

Instead, we believe that through adoption of sound business and management practices, accompanied by regulatory reform, the Postal Service can improve its performance in its current markets and follow the technological curve into the new communication opportunities.

However, to do this we believe that there are four areas where various reforms are required. I would like to focus briefly on these before concluding my remarks. I'll say my colleagues from the DMA and AMMA will provide you with further elaboration, including specific recommendations that our industry believes will increase the efficiency and improve the service quality of the USPS.

First, L.L.Bean requires service that is timely, reliable and consistent. It is necessary for the Postal Service to adapt specific quantifiable performance standards that are relevant to the various customer segments to which it provides services, and publicly report their performance in meeting those standards. And there is a say-

ing in total quality management, "If you don't measure it you can't improve it."

When this has been done by the Postal Service, our experience is that service quality improves considerably. For example, we have worked in a partnership with the Postal Service in the northeast to improve the timeliness with which our catalogs are delivered to meet a performance standard that is very important to us. This effort has resulted in a 30 percent improvement in the percentage of catalogs that are delivered within a 3-day window. This is an increase in productivity, pure and simple, and one which will benefit other Postal Service customers, not just L.L.Bean's.

Second, we believe that it is time to permit the Postal Service greater latitude in managing its internal operations to respond to changes in its market in establishing alternative compensation options to improve overall performance and in increasing its use of contracting for specific services to improve efficiency and stimulate innovation. In addition, investments in innovative technologies and automations must continue to mitigate anticipated cost increases.

Third, we have learned that consumers will not tolerate specific increases in prices, and thus to remain competitive our average price increase in the last 5 years was approximately one half of the CPI. The market will not allow passing on the costs of inefficient suppliers, and the Postal Service is no exception.

To remain competitive, the Postal Service must increase productivity and pass those gains on to its customers in the form of stabilized postal rates. L.L.Bean believes that our markets will become even more competitive and that we will not be able to increase prices of our products over the next 5 years.

We would like to see the Postal Service embrace a similar set of expectations with respect to its prices over the same period. We believe this would stand in marked contrast to the last 8 years, during which L.L.Bean has experienced three significant rate increases that raised our rates 90 percent, or three times faster than the consumer price index. Needless to say, increases such as this make competitive alternatives more viable.

In contrast, an expectation of stable prices would send a very important signal to customers regarding the commitment of the Postal Service to ensure its competitive viability.

Fourth, we believe that the Postal Service must be provided similar flexibility and authority with respect to introduction of new services, especially where those services extend the scope of the Postal Service operations to new markets.

One example of this is our recent decision to award the USPS with our Japan parcel business. We asked nine companies to bid on our business, address our need to improve delivery time, cut costs and provide greater service to our customers. The Postal Service acted quickly to our request, improved package delivery time by 50 percent and provided tracking and tracing capability that we required. When given the opportunity to compete, the Postal Service can respond.

The intent of these four areas of reform should be to ensure that both the internal and external rules and systems governing the Postal Service operations are designed to permit the Postal Service

to function in a more business-like manner and thus to compete more effectively for its customers.

We appreciate that this set of reforms presents considerable challenges and that as a whole must be phased in and monitored very closely. We believe reforms must be implemented which are designed to promote innovation and instill a new level of cost-consciousness and market responsiveness in the Postal Service.

In conclusion, I come here today not as a postal expert or a visionary for the electronic super highway, but rather as a concerned customer of the USPS.

I want to express my company's appreciation to this Committee for the opportunity to share our thoughts and ideas on matters that are so vital to our success.

We believe that the next 5 years will be critical years for the USPS. The United States Postal Service continues to play a critical role in the conduct of business and defining the social fabric of this country. I have expressed in prior testimony L.L.Bean's desire that the Postal Service remain one of our most valued partners and to this end have pledged our full commitment to work with the Postal Service over these next 5 years to help it prepare for and meet the difficult challenges it faces. In fact, L.L.Bean was one of several companies which participated in the Postal Service's FuturePost conference last July.

I'm here today to offer the same pledge to this Committee as you work to define the mission, organization, operations and environment of the Postal Service.

Thank you, Senator, and I'll be happy to answers any questions.

[The prepared statement of Mr. McCormick follows:]

PREPARED STATEMENT OF CHRISTOPHER McCORMICK

Chairman Stevens, members of the Committee, my name is Christopher McCormick, and I am the senior vice-president for L.L.Bean, Inc. located in Freeport, Maine.

As most of you are probably aware, L.L.Bean is the largest catalog retailer in the Sporting Specialty field. We provide a wide range of products that allow our customers to pursue and enjoy their outdoor activities. L.L.Bean believes very strongly in providing our customers with fully tested quality products and superior customer service. After all, it takes a great deal of trust for a customer in Fairbanks, for example, to place an order for a pair of hunting boots with a company located in Maine.

In addition, if that customer in Fairbanks is not satisfied, it is very expensive for us to correct a mistake. Thus, we learned very early on that there is no substitute for "getting it right the first time" and that getting it right means satisfying the needs and expectations of our customers.

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L.L.Bean interacts daily with its customers in four (4) critical respects:

- First, through our marketing efforts, we attempt to make customers aware of our company and the full range of products we provide.
- Second, our order processing facilities receive thousands of orders each day from our customers.
- Third, we must fulfill the orders we receive from our customers and ensure that the products they purchase are delivered reliably and expeditiously.
- And finally, we must provide our customers with a level of service that will earn their trust and encourage them to continue to buy our products.

The ways in which we interact with our customers involve technologies and processes that are constantly changing. Indeed, L.L.Bean is continuously searching for new and better ways to interact with our customers to ensure that the shopping experience meets or exceeds their expectation. After all, our customers have many al-

ternatives—this is the only way we can ensure that they will continue to shop with us in the future.

Historically, virtually 100 percent of our interactions with our customers in each of the four areas I have mentioned occurred through the U.S. Postal Service.

In fact, when Parcel Post was introduced in 1912 by the U.S. Postal Service, a pair of "L.L.'s" hunting boots were in the first parcel to leave the Freeport Post Office. Over time, however, in order to remain competitive in our business, we have responded to the demands of our customers by shifting various aspects of our operations to alternative technologies or competing vendors.

One significant shift away from the U.S. Postal Service occurred with the advent of "800" service 10 years ago. Our customers told us that they wanted faster service, direct access to our order processing facilities, and more information about our product line. We responded with the now commonplace "toll-free" ordering system.

Because this system better met the needs of our customers, it has grown continuously since its introduction. In fact, 10 years ago, customer orders were split approximately 80 percent U.S. mail and 20 percent telephone. Today, the split is the reverse, and we expect that over the next 5 years, our "800" service will account for 95 percent of our incoming orders.

The second shift away from the U.S. Postal Service has occurred more recently, as we moved our order fulfillment activities from the Postal Service to UPS and now Federal Express. As with "800" service, we have made this move, because our customers demanded superior quality services at the best possible prices. Interestingly, Federal Express has met our customers' needs through its superior use of information technology. The consequence to the Postal Service has been the loss of $45 million per year in revenues.

The third major shift has yet to occur, but when it does, it will revolutionize our industry and our relationship with our customers. As a catalog marketer, L.L.Bean relies upon catalogs to provide our customers with information about the products we sell. This past year, for example, we mailed over 140 million catalogs to some 25 million households. To do this, we rely on the Postal Service, just as we have since our first catalogs were distributed 84 years ago. L.L.Bean, however, cannot remain stagnant as our customers change and impose new demands on us and our competitors. For example, this past year, we experimented with limited broadcast advertising to reach customers in key market segments, in an efficient and timely fashion.

We have also undertaken an aggressive program of exploring the use of electronic media, such as CD–ROM technology, and we are very interested in the potential of the Internet as a future communications channel with our customers.

In fact, this past October, we established our own "Website" and are already having difficulty keeping up with the demands being placed on the site. In January alone, we had over 60,000 "visitors" to the site, approximately 15,000 of whom were international visitors, two-thirds of whom were from Japan. Since its inception, we have taken thousands of catalog requests and orders just in the first 6 months of operation.

Perhaps as telling as the number of visitors we have had, have been the suggestions they have left. These customers are telling us that they want to order merchandise on-line; that they would like more information on our products, services and outdoor activities; that this is a more convenient way for them to shop; and that they are very capable of using the technology.

An important business maxim for any retailer is "listen to your customers." At L.L.Bean, we steer by this principle. Many of our customers are now equipped and ready to enter a new age of communication and we must be ready as well.

We cannot afford to ignore what these customers are telling us. Nor can we afford to underestimate the urgency with which we must respond.

The telecommunications legislation you recently enacted is already being felt in our marketplace. AT&T's recent announcement of its intent to provide unlimited Internet access to its customers for $20 per month may have the same effect on our new generation of customers as its introduction of "800" service had on their parents a generation ago.

Whether we like it or not, the simple fact is that technology is rapidly becoming the driving force defining our interactions with our customers. And, Bean must be prepared and well positioned in our marketplace to capitalize on new and more effective ways to serve our customers—or we will be left behind like many once-successful businesses that could not adapt to their changing marketplaces.

Imagine having the ability to obtain greater information whenever you need it about a product, download a video demonstrating how the product was made or to be used and having recommendations on where one can use it—National Parks,

camps or the best fishing locations. Providing new value-added services like this is the new competitive arena—and the last one in . . . loses.

Our operations and experiences are not dissimilar from those of other firms in the Direct Marketing Industry, and as such, have profound implications for the U.S. Postal Service. Postmaster General Runyon recognizes the competitive pressure the Postal Service faces. In a recent speech he stated, ". . . our competitors are beating us, and beating us soundly in about every area of our business . . . Of our six major product areas, we are losing share in all but one."

The trends in our industry that have resulted in a loss of market share for the Postal Service are now threatening the remaining area in which it has retained its competitive advantage—standard mail services—specifically, catalog distribution.

While the competitive threat to the Postal Service is real and growing, the consequence does not have to be a continuing erosion of market share and financial instability. Instead, we believe that through the adoption of sound business and management practices, accompanied by regulatory reform, the Postal Service can improve its performance in its current markets and follow the technological curve into new communications opportunities.

However, to do this, we believe that there are four (4) areas where various reforms are required. I would like to focus briefly on these before concluding my remarks. My colleagues from the DMA, AMMA and MOAA will provide you with further elaboration, including specific recommendations that our industry believes will increase the efficiency and improve the service quality of the U.S. Postal Service.

First, L.L.Bean requires service that is timely, reliable and consistent. It is necessary for the Postal Service to adopt specific, quantifiable performance standards that are relevant to the various customer segments to which it provides services and publicly report their performance in meeting those standards. There's a saying in Total Quality Management.—"If you don't measure it you can't improve it."

Where this has been done by the Postal Service, our experience is that service quality improves considerably.

For example, we have worked in partnership with the Postal Service in the Northeast to improve the timelines with which our catalogs are delivered, to meet a performance standard that is very important to us. This effort has resulted in a 30 percent improvement in the percent of our catalogs that are delivered within a 3-day window. This is an increase in productivity, pure and simple and one which will benefit all Postal Service customers, not just L.L.Bean.

Second, we believe that it is time to permit the Postal Service greater latitude in managing its internal operations to respond to changes in its markets, in establishing alternative compensation options to improve overall performance, and in increasing its use of contracting for specific services to improve efficiency and stimulate innovation. In addition, investments in innovative technology and automation must continue to mitigate anticipated cost increases.

Third, we have learned that consumers will not tolerate significant increases in prices. And thus, to remain competitive, our average price increase in each of the last 5 years was approximately one-half the CPI. The market will not allow passing on the costs of inefficient suppliers—the Postal Service is no exception.

To remain competitive, the Postal Service must increase productivity and pass those gains on to its customers in the form of stabilized postal rates. L.L.Bean believes that our markets will become even more competitive, and that we will not be able to increase the prices of our products over the next 5 years. We would like to see the Postal Service embrace a similar set of expectations with respect to its prices over this same period.

We believe this would stand in marked contrast to the last 8 years during which L.L.Bean has experienced three significant rate increases that raised our rates 90 percent or three times faster than the increases in the Consumer Price Index. Needless to say, increases such as this make competitive alternatives more viable. In contrast, an expectation of stable prices would send a very important signal to customers regarding the commitment of the Postal Service to ensure its competitive viability.

In addition to overall price stability, we believe that the Postal Service must be provided with more flexibility in establishing prices for its services, especially for those services that are subject to effective competition. As I noted earlier and as I know others will emphasize, the Postal Service must be provided the tools to compete in those markets where alternative providers or new technologies are threatening to hemorrhage its financial condition.

Fourth, we believe that the Postal Service must be provided similar flexibility and authority with respect to the introduction of new services, especially where those services extend the scope of Postal Service operations to new markets.

One example of this is our recent decision to award USPS with our Japan parcel business. We asked nine companies to bid on this business and address our need to improve delivery time, cut costs and provide greater service to our customers.

The Postal Service acted quickly to our request—improved package delivery time by 50 percent and provided tracking and tracing capability that we required. When given the opportunity to compete, the Postal Service can respond.

The intent of these four areas of reform should be to ensure that both the internal and external rules and systems governing Postal Service operations are designed to permit the Postal Service to function in a more business-like fashion and thus to compete effectively for its customers.

We appreciate that this set of reforms present considerable challenges, and that as a whole, must be phased in and monitored very closely. We believe reforms must be implemented which are designed to promote innovation and instill a new level of cost—consciousness and market responsiveness in the Postal Service.

While certainly difficult, we believe that these reforms are possible—indeed, the recently enacted telecommunications legislation embraces many of these same reforms. With diligence, hard work, cooperation and commitment, you have been able to overcome many of the same types of challenges in the telecommunications arena and thereby create landmark legislation that will power our economy into the next century.

We hope that you will focus the same effort on the Postal Service and achieve the same level of success.

In conclusion, I came here today not as a Postal expert or visionary for the new electronic super highway, but rather as a concerned customer of the USPS.

I want to express my Company's appreciation to this Committee for the opportunity to share our thoughts and ideas on matters that are so vital to our success. We believe that the next five (5) years will be critical years for the U.S. Postal Service. If the reforms that I have discussed are not implemented and as a result the Postal Service is unable to meet the needs of its customers in its existing as well as developing markets, we believe that it will lag behind the technological curve and suffer from continuing financial instability.

The United States Postal Service continues to play a critical role in the conduct of business and in defining the social fabric of our country.

I have expressed in prior testimony, our desire that the Postal Service remains one of our most valued partners, and to this end, have pledged our full commitment to work with the Postal Service over these next 5 years to help it prepare for and meet the difficult challenges it faces.

In fact, L.L.Bean was one of several companies which participated in the Postal Service's FuturePost conference last July.

I am here today to offer that same pledge to this Committee as you work to redefine the mission, organization, operations and environment of the Postal Service.

Thank you for your time and attention. I would be happy to answer any questions you might have.

Chairman STEVENS. Thank you very much.

Mr. Gitlitz, I'm interested in the draft that you have submitted, and I thank you for the efforts your people have made to prepare it. It is somewhat unique. I do have a couple questions for you on that.

My good friend is here now so that I may go to the other hearing, but let me just ask you some general questions. You are all substantial users of the Postal Service now, do you all agree that we should have a monopoly in first-class mail for the Postal Service into the future?

Mr. GITLITZ. I certainly think, Senator, in the short term——

Chairman STEVENS. Pardon me, I have cut out Mr. Baer.

Mr. Baer, do you have a statement?

Mr. BAER. Yes, I do, Senator.

Chairman STEVENS. Please continue.

TESTIMONY OF CARY BAER, VICE PRESIDENT, DELIVERY SERVICES, THE READER'S DIGEST ASSOCIATION, INC.

Mr. BAER. Thank you, Mr. Chairman, Senator Smith.

My name is Cary Baer, vice president of Delivery Services for Reader's Digest USA and a member of the DMA Government Affairs Committee.

Chairman STEVENS. Would you excuse me? I do have to go to the other committee, and I will come back in time for some questions.

Mr. BAER. Thank you.

Previously at Reader's Digest, I was vice president of Global Postal Affairs, so I have some knowledge of postal services outside of the United States.

Reader's Digest is a global publisher and direct marketer of magazines, books, and home entertainment products, with the worldwide postal expense of several hundred million dollars, so we think we know things postal. And our postal expense in the United States is relatively balanced across all classes of mail.

Let me say first that based on my own experience and observation of the U.S. Postal Service, considering its overall level of service and rates, it is the best postal service in the world.

And, Mr. Chairman, I commend you for holding these hearings, because their purpose, as I understand it, is to enact legislation as appropriate to help ensure that the U.S. postal system maintains that No. 1 position among the world's postal services and continues to provide what this country needs from its postal service.

Well, what is it that this country, its citizens and the business environment, needs from the Postal Service?

In my view the needs are simple and straight forward. The country does and will continue to need a hard copy delivery service that provides universal consistent delivery with a reasonable degree of speed and a reasonable price.

In my view, we will need to see in the years ahead a Postal Service that is smaller in staff complement, providing delivery service that is at least as fast as today, but far more consistent, with rates not much different than today, perhaps even lower than today's rates.

In my opinion, unless this vision becomes reality, the U.S. postal system will be on a slippery slope downward toward a very tortured future.

First let me describe a few of the serious problems that the USPS faces.

No. 1, an accelerating decline in mail volume. Usage by businesses and individuals of electronic funds transfer and electronic data transfer has begun in earnest and will accelerate rapidly. Electronic banking and electronic consumer bill payment is in its infancy but will rapidly take off.

Some speculate that electronic banking will follow the same growth curve as facsimile. Recall that the facsimile machine had a slow start but is now indispensable. Just about every business card has a FAX number on it.

Recall also that when facsimile began it was not considered to be a threat to postal volume. In fact, the prior Postmaster General, when asked about the impact of facsimile on mail volume, stated that almost all facsimiles concluded with the statement, "Hard copy

to follow." When was the last time any of us saw that on a facsimile that we received?

And since more than half of postal revenue comes from first-class mail, with a significant portion related to and caused by financial transactions, the switch to electronic funds transfer and electronic banking will have a significant and very negative effect on posting revenues.

No. 2, relatively static productivity. In spite of large capital investments in mail processing equipment, annual postal productivity improvements have been modest, to say the least. In fact, USPS productivity often trails the rate of productivity improvement in the United States.

No. 3, compensation does not keep pace with responsibility or success. Senior level compensation at the Postal Service trails that at equivalent levels of responsibility in the private sector. In addition, the private sector usually has significant opportunities for incentive compensation based on results. For all practical purposes, these opportunities do not exist at the Postal Service.

Mr. Chairman, now that I have stated very briefly what I see as some of the more significant problems facing the Postal Service, I would like to make several specific suggestions for change that in my view would provide the Postal Service with some of the tools necessary to be what it must become.

No. 1, flexibility to compete. The Postal Service is in a very competitive environment but has very limited flexibility to compete and change as the competitive environment changes.

Therefore, I recommend that as a beginning the Postal Service be given freedom and flexibility in the non-monopoly mail categories, specifically parcel post and express mail. For these types of mail, the Postal Service has a very small market share and is among the least significant players in the market place, yet it has the greatest degree of regulatory control over its pricing and products.

Clearly, it is a very strange environment that permits postal competitors, with their overwhelming market share, to participate and question the Postal Service in hearings at the Postal Rate Commission with their clear objective to raise postal rates even higher than the Postal Service asks for. The ability to have competitive pricing and product development will begin to provide the Postal Service with the experience necessary to compete in the market place. No doubt, there will be some stumbling along the way, but the Postal Service must be given this flexibility.

I would permit the Postal Rate Commission to exercise some regulatory oversight in these competitive classes, but primarily as an auditor rather than as a rate setter.

No. 2, productivity through incentives and competition. One of the major reasons for the lack of productivity at the USPS is due, in my opinion, to the poor working relationship between the USPS management, including supervisors, and the craft employees.

I offer no opinion as to who is at fault, if anyone. The fact of the matter is that the working environment is clearly not good. It demonstrates itself in the high number of grievances filed and kept open for so long. The Postal Service will be unable to properly ad-

dress its external competitors if it is unable to solve its internal labor strife.

Here I would make two suggestions. First, the Postal Service and its unions need to find a way to get along. To assist them in that process, I would introduce a meaningful productivity and profit sharing system similar to that which is working so successfully in the automobile industry, particularly at Chrysler.

As part of a previous postal labor settlement, something called STET was introduced, and I have a copy of the Striving for Excellence Program back in the fall of 1990. This program has not, to my knowledge, had any impact on the Postal Service, primarily because the two largest unions have chosen not to participate. I believe it is a serious mistake on their part. I have been told that the unions feel that STET would replace annual salary increases. In my view, STET should be over and above whatever increases are negotiated at that bargaining table.

However, STET incentives should be paid only if real bottom line productivity improved, using as a measurement basis total pieces of mail processed per year per person. If there were to be meaningful productivity improvements, my company, as a major postage payer, would be willing to financially share some of that productivity savings through STET payments.

Second, although today's postal competitors are real, they are not as visible to the postal employee as they need to be to promote real change. Many postal employees feel that as long as the private express statutes and the mailbox exclusion rule are in place, the Postal Service is safe.

Clearly, electronic competition ignores the mailbox, but its lack of visibility causes these regulations to act as a false crutch to the postal employees. We know that competition promotes positive change and works in the economy at large.

I would recommend to the Postal Service that in selective ways, perhaps in selected areas the Postal Service ease the private express statutes and/or the mailbox exclusion rule so that postal competition can be more visible to the employees.

If the Postal Service does not learn how to compete successfully in a mailbox, it will never learn to compete against the more significant competitors in the electronic world.

It was interesting, this morning in *U.S.A. Today* on the front page, the bottom, there is an electronic print media snapshot, and it poses the question, "Plans by newspapers and magazines to distribute at least part of their publication electronically; 25 percent already do, and within 2 years another 31 percent plan to, and another 19 percent plan to within 5 years." So the movement is certainly there not only for electronic bill payments but electronic print media.

It should be noted that some of the most progressive and successful postal services around the world do not restrict competition through these exclusionary rules.

No. 3, the current cap on compensation has an impact on the Postal Service's ability to compete in the managerial market place. Here I would recommend a lifting of the cap to some higher compensation level.

What I would do, however, is to maintain the current direct salary limit, but permit postal employees to get a bonus compensation of perhaps up to 30 percent of their salary based on the USPS's attainment of productivity, financial, delivery service goals, and the individual managers' attainment of their written business objectives.

The Board of Governors should monitor this system. This pay for performance compensation is very much in use in the private sector. When it is working properly, it helps ensure that individual goals and objectives are in unison with corporate goals and objectives.

Mr. Chairman, that concludes my thoughts on legislative changes that could assist the Postal Service in maintaining its position as part of the vital infrastructure of the United States.

Some have said that the likelihood of legislative change has been reduced because of recent solid postal financial performance. Often we forget, however, that a rate increase can appear to cover a lot of problems. I trust, however, that the Congress will utilize these hearings to develop legislation that will have a positive impact on the Postal Service, its employees and its customers.

Thank you, and I look forward to answering any questions that you may have.

[The prepared statement of Mr. Baer follows:]

PREPARED STATEMENT OF CARY H. BAER

Mr. Chairman and Members of the Subcommittee, my name is Cary Baer, Vice President of U.S. Delivery Services for Reader's Digest USA and a member of the DMA Government Affairs Committee. Previously at Reader's Digest, I was Vice President of Global Postal Affairs so I have some knowledge of Postal Services outside the United States.

Let me say first that based on my own experience and observation, the U.S. Postal Service, considering its overall level of service and rates, is the best Postal Service in the world.

However Mr. Chairman, I commend you for holding these hearings because their purpose, as I understand it, is to enact legislation as appropriate to help ensure that the USPS maintains that No. 1 position among the worlds postal services and continues to provide what this country needs from its Postal Service.

What is it that this country, its citizens and the business environment needs from the Postal Service?

In my view the needs are simple and straight forward; the country does and will continue to need a hard copy delivery system that provides universal, consistent delivery with a reasonable degree of speed, at a reasonable price.

In my view, we will need to see in the years ahead a Postal Service that is smaller in staff complement, providing delivery service that is at least as fast as today but far more consistent, with rates not much different than today—perhaps even lower than today's rates.

In my opinion, unless this vision becomes reality the USPS will be on a slippery slope downward to a very tortured future.

First, let me describe a few of the serious problems that the USPS faces.

1. Accelerating decline in mail volume.

Usage by businesses and individuals of electronic fund transfer and electronic data transfer has begun in earnest and will accelerate rapidly. Electronic banking and consumer electronic bill payment is in its infancy but will rapidly take off. Some speculate that electronic banking will follow the same growth curve as facsimile. Recall that the facsimile machine had a slow start but is now indispensable. Just about every business card has a fax number on it. Recall also that when facsimile began it was not considered to be a threat to postal volume. A prior PMG, when asked about the impact of facsimile on mail volume, stated that almost all facsimiles concluded with the statement "hard copy to follow". When was the last time any of us saw that on a facsimile we received?

Since more than half of postal revenue comes from First-Class mail, with a significant portion related to and caused by financial transactions, the switch to electronic funds transfer and electronic banking will have a significant and very negative affect on postal revenues.

2. Relatively static productivity.

In spite of large capital investments in mail processing equipment, annual postal productivity improvements have been modest to say the least. In fact, USPS productivity often trails the rate of productivity improvement in the United States.

3. Compensation does not keep pace with responsibility or success.

Senior level compensation at the Postal Service trails that at equivalent levels of responsibility in the private sector. In addition, the private sector usually has significant opportunities for incentive compensation based on results. For all practical purposes these opportunities do not exist at the Postal Service.

Mr. Chairman, now that I've stated very briefly what I see as some of the more significant problems facing the Postal Service, I would like to make several specific suggestions for change that in my view would provide the Postal Service with some of the tools necessary to be what it must become.

I. Flexibility to Compete

The Postal Service is in a very competitive environment but has very limited flexibility to compete and change as the competitive environment changes. I, therefore, recommend that as a beginning the Postal Service be given pricing freedom and flexibility in the non-monopoly mail categories, specifically Parcel Post and Express Mail. For these types of mail, the Postal Service has a very small market share and is among the least significant players in the market place. Yet it has the greatest degree of regulatory control over its pricing and products.

Clearly it is a very strange environment that permits postal competitors with their overwhelming market share to participate and question the Postal Service in hearings at the Postal Rate Commission with their clear objective to raise postal rates even higher than the Postal Service asks for.

The ability to have competitive pricing and product development will begin to provide the Postal Service with the experience necessary to compete in the market place. No doubt there will be some stumbling along the way, but the Postal Service must be given this flexibility.

I would permit the Postal Rate Commission to continue to exercise some regulatory oversight in the competitive classes, but primarily as an auditor rather then a rate setter.

II. Productivity Through Incentives and Competition

One of the major reasons for the lack of productivity at the USPS is due, in my opinion, to the poor working relationship between USPS management (including supervisors) and the craft employees. I offer no opinion as to who is at fault, if anyone. The fact of the matter is that the working environment clearly is not good. It demonstrates itself in the high number of grievances filed and kept open for so long. The Postal Service will be unable to properly address its' external competitors if it is unable to solve its internal labor strife.

Here I would make two suggestions. First, the Postal Service and its unions need to find a way to get along. To assist them in that process, I would introduce a meaningful productivity and profit sharing system similar to that which is working so successfully in the automobile industry, particularly at Chrysler.

As part of a previous postal labor settlement "STET" was introduced. This "Striving for Excellence Together" program has not, to my knowledge, had any impact on the Postal Service, primarily because the two largest unions have chosen not to participate. I believe it is a serious mistake on their part. I've been told that the unions feel that STET would replace annual salary increases. In my view, STET should be over and above what ever increases are negotiated at the bargaining table. However, STET incentives should be paid only if real bottom line productivity improved, using as a measurement basis total pieces of mail processed per year per person.

If there were to be meaningful productivity improvements, my company as a major postage payer would be willing to financially share some of that productivity saving through STET payments.

Secondly, although today's postal competitors are real they are not as visible to the postal employee as they need to be to promote real change. Many postal employees feel that as long as the private express statutes and the mailbox exclusion role are in place, the Postal Service is safe. Clearly electronic competition ignores the mailbox, but its lack of visibility causes these regulations to act as a false crutch to postal employees.

We know that competition promotes positive change. It works in the economy at large.

I would recommend that in selected ways, perhaps in selected areas, the Postal Service ease the private express statutes and/or the mailbox exclusion rule so that postal competition can be more visible to the employees. If the Postal Service doesn't learn how to successfully compete in the mailbox, it will never learn to compete against the more significant competitors in the electronic world. It should be noted that some of the most progressive and successful postal services around the world do not restrict competition through these exclusionary rules.

III. Compensation

The current cap on compensation has an impact on the Postal Service's ability to compete in the managerial marketplace.

Here I would recommend a lifting of the cap to some higher compensation level. What I would do however, is to maintain the current direct salary level limits but permit postal employees to get bonus compensation up to perhaps 30 percent of their salary based on the USPS' attainment of productivity, financial and delivery service goals and the individual managers attainment of their written business objectives. The Board of Governors should monitor this system. This pay for performance compensation is much in use in the private sector. When it is working properly it helps ensure that individual goals and objectives are in unison with corporate goals and objectives.

Mr. Chairman, that concludes my thoughts on legislative changes that could assist the Postal Service in maintaining its position as part of the vital infrastructure of the United States.

Some have said that the likelihood of legislative change has been reduced because of recent solid postal financial performance. Often we forget, however, that a rate increase can appear to cover a lot of problems. I trust, however, that the Congress will utilize these hearings to develop legislation that will have a positive impact on the USPS, its employees and its customers.

Thank you, Mr. Chairman, and I look forward to answering any questions that you may have.

OPENING STATEMENT OF SENATOR SMITH

Senator SMITH. [Presiding.] Thank you very much, Mr. Baer.

Senator Dorgan, this is the first panel. Did you have an opening statement?

OPENING STATEMENT OF SENATOR DORGAN

Senator DORGAN. Let me ask unanimous consent to put my opening statement in the record?

Senator SMITH. Without objection.

[The prepared opening statement of Senator Dorgan follows:]

PREPARED OPENING STATEMENT OF SENATOR DORGAN

Thank you, Mr. Chairman, for holding these 2 days of hearings. As this Subcommittee considers how we might improve America's postal system, it is important that we hear from customers who depend on mail delivery that is speedy, reasonably priced and universal.

I want to mention two points at the outset of these hearings. The first is that these hearings are entitled "Conversations with Customers." That's fine: We need to have these conversations. But there's another set of conversations we need to have as well. This Subcommittee needs to hear from postal workers.

Companies all across America are restructuring themselves to respond to employees' suggestions for improvement and to give workers greater responsibility for their work. It would be strange indeed if this Subcommittee were to ignore the best private sector management practices and not ask postal workers how they feel about various reform proposals. Workers on the front line can tell us how the postal system works on a day-to-day basis, what is wrong, and what could be done to fix it better than anyone else can. So I would hope, with the greatest respect, that the Chairman will consider holding another day or two of hearings entitled "Conversations with Workers."

The only other point that I want to raise is that we should strive for the best and most accurate data to understand today's Postal Service. I have been somewhat surprised by some of the conclusions that today's witnesses draw from numbers they cite in their prepared statements. I will be asking questions to try to clarify the productivity and rate statistics.

Thank you again, Mr. Chairman, for holding these hearings. I look forward to our witnesses' testimony, and I look forward to working with you on a postal reform bill that ensures speedy, reasonably priced universal service.

Senator SMITH. When I came in and listened to you gentlemen, I'm reminded of a story that has been drifting around Capitol Hill for a number of months, but it is certainly humorous. I don't know if it ever got out into the public domain.

But Senator Craig had received a letter about 6 or 8 months ago that actually the post office had delivered, so this is not a rap at the post office. But somewhere it got lost in one of these walls around here. It was tucked behind a bureau or something and never got delivered. It was mailed in 1912 to Senator Bora, and the letter indicated that this gentleman was a farmer out in Idaho someplace and his cows were dying and he wanted to know what the latest remedy for this type of disease was that the Government could provide him.

So since Senator Bora had long since died, and I'm sure all the cows died, I can imagine every time one of those cows died he was cussing poor Senator Bora for not ever getting back to him.

But as a person who really is not all that sophisticated in all this technology but is trying—I have a computer and try to communicate somewhat with that—I'm just fascinated by all of this and where the post office will be in this in 10, 15 or 20 years, or even now.

I noted, Mr. Baer, your comparison of electronic banking and bill payment capability to the growth curve of the FAX. I think you are right. This is going to have a major impact. And any of you could comment.

But from your own perspective, is there anyway that the Postal Service could, or even should, become a player in this market? I'd be interested in your responses, just briefly.

Mr. VOLNER. Mr. Chairman, when I came to Washington I came to work for the FCC and I was told, don't go into radio because radio is going to be obsolete in 5 years. And then I was told, don't go into television because television is going to be obsolete in 5 years because it is going to be overtaken by cable. And now people are saying don't go into cable, for God sakes, you have got to go into the new high-tech stuff.

The Postal Service can exist side by side with all of these alternative information delivery systems. They create opportunities for the Postal Service, as well as competitive threats. The question is not whether the Postal Service will survive, the question is can we give it the means so that it can compete in those markets that it is able to do so, and so that as an alternative it is flexible, cost effective, efficient, all of the things that Mr. Baer and Mr. McCormick were talking about.

Senator SMITH. Anyone else want to comment?

Mr. GITLITZ. I just think that we are very conscious of the role that the new media will play in direct marketing. It is going to offer a lot of choices for marketers. I don't think it is going to sup-

plant anything, as we said in our statement, it is going to add to the marketing mix much as television didn't replace magazines, and I don't think the new media will replace mail.

But to your question, I think it is incumbent on the Postal Service to get its core business straightened out first and be concerned with managing costs, with reasonable rate increases, before it embarks on chancy new services.

I think there are some new things, however, that they can do that are related to their core business, and I would think that that's what they ought to concentrate on first.

Senator SMITH. There is an irony here. There is kind of a dichotomy. Right now the Postal Service raises its money by selling postage.

How would you suggest that they raise the funds to move into this technology range? If you are moving away from the stamp, you really can't do it with selling postage stamps, can you? I mean, there has got to be some change.

What changes would you suggest they make or we make to help them in this competition, if any?

Mr. BAER. Well, I think the Postal Service in its current environment, it still is a business that generates revenues of $55 billion. So even if there was some reduction in it, I think it is going to be a very significant business for a good number of years, at least as far ahead as we can see.

I think the issue on the table is how to compete in the marketplace against its current competitors as well as the electronic ones, and I think in terms of its electronic ones, I don't believe it can compete directly against the electronic customers, but I think if it provides service that is more consistent than today, and it doesn't change its rates for a good number of years, and perhaps even lowers them, I think that it will maintain a significant volume of business, and then maybe it could get into some other businesses.

Certainly the postal services around the world have used some of their retail network to provide governmental services. I know the Postmaster General is looking at that.

So it has a large network. It needs to make it more efficient and more consistent than it is today with the flexibility that its nonregulated competitors have.

Senator SMITH. On another matter, Mr. Volner, you seemed to imply in your comments, your record comments, that the Postal Service monopoly should be removed.

Are you saying that?

Mr. VOLNER. Over the long term, it is possible that we might have to deal with the question of a monopoly. In the short run, as Mr. Gitlitz and others have said many times, you can't just pull that monopoly off and expect things to work rationally.

Those of us who have lived through the telecommunications revolution recognize that it was only 20 years ago that AT&T had a complete monopoly on long distance services. And it took us a long time.

I wouldn't even think about doing anything about the monopoly right now. Our short-term goals are to give them flexibility, to leave them with the monopoly, and to leave rate regulation in place in a more relaxed form.

What the future holds, let's see how they do in a more relaxed environment before we decide what the final solutions are. There are no final solutions in this business.

Senator SMITH. I have heard Senator Dorgan say, I believe, that he is from a town of 200 or 300 people in North Dakota.

Supposing it just wasn't a good day to get the mail out there to Senator Dorgan in North Dakota, or his wife or children, or whoever lives in that town.

How would you respond to that?

Mr. VOLNER. One of the reasons that we are suggesting that the monopoly be left in place is that the question of how you resolve the matter of universal service in a completely unregulated environment is a very serious problem. It is not just Senator Dorgan who has that problem. Senator Stevens also has that problem on a kind of macro level.

We all have that problem. All AMMA members need to deliver mail around the country. And so long as it appears that we need a monopoly in order to maintain universal service, let's leave it there. That's not a part of our agenda.

Indeed, what I was trying to say in our prepared statement was let's not worry about the monopoly now, let's worry about what we can do now and deal with the future. I mean, when we began the breakup of AT&T none of us had dreamed what was going to emerge. But the time was right. We had enough information to know that some things could be broken up.

The time is not right here.

Senator SMITH. Senator Dorgan.

Senator DORGAN. Mr. Chairman, thank you very much. I have not read in detail all of your statements. I regret that I wasn't able to be here for the first part of the hearing. I had another meeting.

Postal reform is an interesting issue. I guess you all represent interests that send out a lot of mail. If other Americans have their mailboxes filled as mine is filled every single day, with stuff from pen pals I have never written to, there is a lot of mail being hauled in America.

Let me ask you a couple of general questions in order to get to the specifics.

Setting aside price just for the moment, is our mail system in this country among the best in the world or is it near the worst in the world? In other words, if you wanted to have a high degree of confidence that a piece of mail would get where it ought to go, would you mail it in the United States, or Honduras, or Czechoslovakia, or where? Where would one want to send mail to have a high degree of confidence that it is going to get where it is intended to go?

Mr. BAER. Mr. Chairman, I'm with Reader's Digest and we do operate in probably 30 or 40 countries around the world.

You preferenced your question by if price is not an issue.

Senator DORGAN. Right. I'm going to come back to price, but I'm talking now about——

Mr. BAER. If price is not an issue, there are a number of countries in which the majority of the population gets overnight delivery, and it is extremely consistent and extremely reliable. They pay a lot of money for it, but the service is outstanding.

Senator DORGAN. And how would you rate the service in our country? Is ours a pretty reliable system?

Mr. MCCORMICK. I would agree with Cary. We also do business in many countries, and I would say definitely our Postal Service is one of the best in the world. I think they are reliable, they are consistent, the quality of service is very good.

But I think they can improve. And keeping away from price for a second, I think they can improve in areas such as better tracking capability of their parcels and be more competitive.

I gave an example in my testimony where we shifted our parcels to Federal Express. One reason why we did that wasn't necessarily due to price, it was due to quality of service. Our customers wanted their package faster, and Federal Express came in and did it in half the time.

So I think our Postal Service is good, and the quality is excellent, but there are better vendors out there.

Senator DORGAN. That's especially true for certain niche services as well. I guess you wouldn't call what Federal Express does a niche any more. But the world has changed and people do want certain kinds of deliveries on an accelerated basis, and they want confidence, and they are willing to pay for that, and so on. I understand that.

But I'm trying to talk about the general run-of-the-mill ability to deliver mail.

Mr. GITLITZ. I think it is also important to point out that while there may be some countries, like in England, where there is overnight delivery, that again, while we are very critical of the Postal Service, we have to comment, in response to your question about how they would rank, we think they do a very fine job, especially when you consider the enormity of our geography, and the enormity of our population, and the volume of mail that is delivered compared to, say, U.K., or France, or even Canada. Canada is a very large country, but their volume doesn't even approach ours.

Mr. BAER. Senator, I said in my testimony that I think when you put everything together—price, service, speed, consistency—the U.S. Postal Service is the best in the world.

Mr. VOLNER. Senator, there is a danger in that question I want to respond to.

In 1968 Western Union was the best overnight information delivery system in the world. Today, it does not exist. And in part it does not exist because changes were happening around it and neither it nor its regulators were willing to respond.

Senator DORGAN. I asked the question without respect to price. Let me ask a question about price now.

It seems to me that there is a relationship between price and service and I want to try to understand a little bit with respect to various kinds of mail whether you think we are paying about the right amount, or overpriced, and then I want to talk just for a moment about the question of competition in certain areas of service with respect to the question of universal service.

Lets talk about price first, and just talk about the first-class service. We all know what we pay to mail a letter first-class in this country.

Are we in line or out of line? Is that sort of generally where you think we ought to be? Is it a fair deal? How does it relate to what has happened to inflation?

Any comments about especially first-class mail?

Mr. BAER. That is a tough question to answer. I think that first-class stamps as probably viewed by most people is OK. It tends to be more a question of what was it a few years ago, what is it likely to be in the years ahead.

After awhile, you begin to accept 32 cents, just as for a long time we accepted 10 cents to make a call on the telephone, and now I guess we accept 25 cents, and it is sort of OK.

Is it as good as it could be? Probably not. And I think that's the issue, and what is it likely to be in the years ahead.

Senator DORGAN. The whole rate setting process with respect to all the classes of mail relates, I assume, to a set of circumstances that deal with all of the costs of the postal system.

And some of you in your testimony have talked about arbitration agreements producing some results that are not appropriate and so on.

The most recent agreements that I'm aware of in the Postal Service have resulted in the salaries rising slightly less than the rate of inflation.

If that's the case generally, would those kinds of results be problematic in terms of rate setting? It would seem to me that that is not part of the problem at this point.

Mr. BAER. I think that the issue, which I believe most of us addressed, is the future. And the competitors are playing in a very different environment. And so the Postal Service needs to—I guess there is a phrase, a lean mean fighting machine, and it needs to get there.

And many people think the problem is wage levels. The wage levels are what they are.

In my view, the problem has to do with the Postal Service's staffing complement and the enormous investment in capital investment in equipment with really very modest productivity improvement.

And if you look just in the world at large and in corporations in the United States, when they make very large investments in capital to add productivity or whatever, they expect to get a significant return for them. That's the return that is missing in the Postal Service.

And, there are a significant number of postal employees who leave every year through normal attrition. And nobody really has to lose their job, they just don't have to be replaced. Yet, in spite of all the capital investments and equipment, the same additional people keep getting rehired.

And that I think is our focus. We need to get a return on that capital investment to keep rates at the level they are, or even lower. That is what seems to be missing in the equation.

Mr. VOLNER. In terms of the rate setting process, I have two comments in response to your question.

In terms of the rate setting process, certainly wage packages below the rate of inflation help, but they are not the whole component, because what really drives rates is not and the wage package

but productivity. If productivity does not come up to expectations, particularly in areas where the Postal Service is engaged in work-sharing, the rates go up too high. And the private sector just can't deal with that.

Senator DORGAN. Well, let me deal with the question that Bob asked about Regent, North Dakota. He has a community like it in his State I'm sure.

I come from a town of 300 people. It is 65 miles south of Dickinson, North Dakota, if anyone knows exactly where that is. It is actually the mid-point in Hettinger County, in case you are still confused.

Those of us from Regent have as great and urgent a need for on-time mail delivery service as does someone living in Washington, D.C. The need is just as urgent.

Now, does it cost a lot more for someone to haul mail to Regent? Perhaps. Because you don't have very many customers there and somebody has got to drive in with some bags of mail, and so it costs a lot more.

But we have decided in this country there are certain things that are of a universal nature, communications and certain other things.

And my guess is that in the postal system—and I'm not an expert in this area—my guess is there are certain areas in the postal system where there are activities that others would say, let's take these activities and compete aggressively, because with these activities there is an enormously profitable potential.

And so if you go to the market system and say, let's take these areas away where there is an income stream that would persuade competitors to come in and compete, which drives down the cost to the consumers, you are left with, I assume, a series of other activities in the postal system that no one wants to compete for because they are losers. They are losers because we, from a universal standpoint, must continue to provide the same service to those people even though it is at a loss. And we offset that loss by revenues in the other areas.

My concerns in talking about all of this are two-fold.

We do have to compete in the future in the postal system, and there are certain things where you are going to have aggressive competition. But you can't ever go off and carve those out without worrying about what happens to the unprofitable area and how do you retain decent service that is equivalent to the service that someone gets in New York City in those small communities.

So I'm not quite sure I understand the answer to all of this, except that I want to be very careful when we start talking about taking things apart here, because I worry about the smaller areas where you will not have competition. No one will want to serve them at a loss.

The genius of the postal system in this country has been we built a very large system, putting together the profitable areas and the unprofitable areas, and merged together they work at a reasonable price to provide pretty good service to everybody in this country.

Having said all of that, Mr. Volner, the point and some others is still an accurate point. There are certain areas where people's needs have changed and they want to develop different patterns of communication, different styles, they are willing to pay more for it.

The postal system must be able to respond to some of these needs. The private sector is competing in some areas. I just want us to be very careful about where we start to weaken the rest of the postal system that the folks in Regent, North Dakota rely on and will rely on for the next 50 to 100 years.

Mr. VOLNER. Senator, your concern is referred to as "cream skimming," that the private sector will come in and take the high profit components, leaving the Postal Service, essentially, forced at outrageous prices to serve the rest of the country.

The answer is, fundamentally at where we stand today, the monopoly should be preserved because that's precisely what the monopoly guards against. None of us have ever advocated complete de-averaging of rates. There is no question that it is in some part our responsibility as commercial mailers to support the price that somebody, in my case, Croton-on-the–Hudson, New York, pays, or in Congressman's McHugh's district, which is also very rural and very remote.

No question there is rate-cost averaging. The question is can you inject some greater flexibility into that without driving the price of the least advantaged categories out of sight? And the answer is certainly you can do that.

I mean, the experience in other countries, and in the telecommunications field, where this debate has been going on for years, establishes that you absolutely can do it. And indeed, if you do it right, what has happened for example with negotiated contracts and long distance, is that the price to the individual consumer has come down, because they are able to generate so much profit by customizing their service to the large user that the remote user is getting the benefit of the rate averaging and his price comes down. It can be done. It cannot be done under the statute as it now stands.

Senator DORGAN. You are absolutely correct with respect to long distance. That is not the case with respect to local service.

Mr. VOLNER. Well, we are just starting local service.

Senator DORGAN. But that will never be the case with local service, and I'll tell you why. I just say axiomatically that it will never be the case with local service. Nobody ever is going to be in a circumstance where we have got eight companies fighting to serve Leffer, North Dakota. It is just not going to happen.

Leffer gets served only because it is part of a larger service area and you can blend areas where you can make some money with areas where you might lose a little money. But on the whole it works as a service area.

So I guarantee you what you say about long distance is absolutely correct. Competition has been a boon to the American consumer in the long distance area. In local service, in telecommunications that will not be the case.

Mr. MCCORMICK. Senator, doing away with the monopoly is radical reform, and I don't think anyone here is asking for radical reform. In fact, if anything, we just said that we are comfortable with the service we are getting with the Postal Service.

So I'm not in favor of radical surgery for this patient today. In fact, I think any reform must include universal service, uniform

rates, and from a business standpoint, we mail 140 million catalogs a year. I'm sure you have seen some of those.

Senator DORGAN. I get most of those, actually. But you are big users, and I think your advice is very important to this Committee.

Mr. MCCORMICK. Picture the complexity though of mailing out 140 million catalogs with one Postal Service. If you start breaking up into baby postal services, the complexity will increase tremendously, and the quality of service I would fear would erode. We can't let that happen.

So I'm not in favor of radical surgery in this patient. I don't think the patient is that sick right now. I think we are just dealing with more moderate reforms, letting the Postal Service compete in the competitive arena more, more flexibility on some of those services and prices, and I think the patient will be better.

Senator DORGAN. Mr. Chairman, I have taken more than my share of the time. The point I made here is that you are very big mailers, you are big users of this system. Your advice is very important, and that's why the Committee has asked for your advice.

My admonition is, yes, we should compete, let's find these areas where we should compete, yes, let's provide some flexibility. Let's also keep our eye on the larger goal of universal service, which I think is very important and it serves this country well, and I don't think you all are disagreeing with that point.

Thank you very much for the testimony you have provided today.

Senator SMITH. Thank you all, gentleman. Unless you have anything else you would like to add, we would like to move on to the next panel. Thank you very much.

Gentlemen, welcome. We have Hamilton Davison, president of the Greeting Card Association, accompanied by Jack Mayer, the vice president for Strategic Planning at Hallmark Cards, and Jeff Weiss, American Greetings Corporation.

We also have Timothy J. May, the general counsel of the Parcel Shippers Association, accompanied by Jerome Jensen, Fingerhut Companies, and Chris Rebello of Current, Inc.

Why don't we start with you, Mr. Davison.

TESTIMONY OF HAMILTON DAVISON, PRESIDENT, GREETING CARD ASSOCIATION

Mr. DAVISON. Good morning, Mr. Chairman. It is a pleasure to be here today to talk on matters that are as important as this. Thank you for giving us this opportunity.

I'm Hamilton Davison, president of the Greeting Card Association. I'm also president and CEO of Paramount Cards in Pawtucket, Rhode Island.

On my right is Jack Mayer from Hallmark Cards in Kansas City, Missouri, and on my far right is Jeff Weiss from American Greetings in Cleveland, Ohio.

With your permission, I would like to read a few brief prepared remarks.

Senator SMITH. All of your statements, of course, will be part of the record, so feel free to summarize.

Mr. DAVISON. The greeting card industry contributes nearly $7 billion in retail sales to the U.S. economy each year, and directly and indirectly employs over a quarter million Americans.

Because nearly two-thirds of all greeting cards are mailed, our future is inextricably bound together with that of the U.S. Postal Service.

Our association has a long history of cooperation and interaction with the Postal Service, dating back to World War II when, as the National Association of Greeting Card Publishers, we helped support the War Bond effort through the sale of Defense Stamp Christmas cards and the sending of V-mail greeting cards.

In more recent times, during Desert Storm and Desert Shield, as an industry we helped bolster troops overseas by contributing greeting cards to school children so they could show their support.

We have performed many collaborative promotions with the Postal Service and we are interested in any initiative to help raise the unit volume of mail.

We have worked with the Postal Service to increase our efficiency. Over the past several years our members have voluntarily eliminated dark colored envelopes from the mail stream. Dark envelope colors inhibit the use of automation technology. And in recognition of that, the Greeting Card Association, also known as the GCA, received the Postal Service's Partners in Progress award.

In the greeting card industry, both collectively and individually, postal matters receive considerable attention, including such issues as the future of the U.S. mail in the electronic information age, people's perceptions of the mail service, and possible solutions to consumers' rising costs of postage.

However, we are not before you today simply to represent the best interests of an industry trade group. We are here advocating the best interest of more than 250 million Americans who use the U.S. mail to send correspondence and news to family and friends.

By the very nature of our product, our vested interest puts us solidly in line with the best interest of the citizen mailer, who we sometimes refer to as Aunt Minnie.

As an industry, we have a history of advocacy for and intervention on behalf of Aunt Minnie.

In addition to a long-standing relationship with the Postal Service, the GCA has appeared before Members of Congress and has represented Aunt Minnie in the regulatory process.

Our customers tell us first-class mail is the most important mail they receive each day. Americans have a deeply rooted sense of their Postal Service. Ask any American about postal matters and you will likely get an ear full of prescriptive suggestions and personal anecdotes.

Most Americans have an individual relationship with their mail carrier, often wishing him or her well as they toil through rain, sleet and snow, particularly this year, making every attempt to deliver to us our mail.

We may not know which Federal tax bracket we belong in, but most every American knows it cost 32 cents to deliver a card or a letter.

We are taught from childhood that first-class mail is specific to each person. You never open up someone else's mail. In fact, focus groups conducted for our industry revealed that Americans believe electronic communications can be intercepted, but that first-class mail is private and secure.

First-class mail is important to people. The Postal Service's own household diary studies confirm this.

What is the first thing that we open when the mail comes? Except at tax refund time when we reach for a distinctive manila envelope, it is the valued personal——

Senator SMITH. I don't get those too often. I don't know about you.

Mr. DAVISON. It is the valued personal correspondence from people dear to us that gets our first attention.

Consumers tell us there are certain tasks that only a letter or a card can perform. The Pony Express is still immortalized in our history and in our popular culture. Most every school-age child knows that Ben Franklin was our first Postmaster. Legal contracts reference serving notice through first-class mail. We communicate with each other through the mail, and we communicate with our Government through the mail.

The post office is, for most, the quintessential governmental symbol, and an institution deeply ingrained in our sense of culture, and an important icon for the United States Government itself.

Going as far back as the Constitution of 1798 and extending to today, the U.S. Postal Service fulfills its congressionally mandated role as provider of a universal communications service, "Binding the Nation together through the correspondence of the people."

Congress knew the letter mailer might be exploited, as when in 1970 you admonished the service not to load costs on to the user for which the service has been given a monopoly.

You established an independent Postal Rate Commission to continue the tradition of checks and balances so critical to the proper functioning of our democracy.

As you intended that the Postal Service serve the interest of the commonweal, you instructed it to be fair and equitable in setting rates, to consider the value of the service to the sender and the recipient, to consider the availability of alternatives, to consider the educational, cultural, scientific and informational content of each piece of mail it handles, and to ensure that one class of mail does not cross-subsidize another.

You created a monopoly in the public interest to serve the public when it communicates. You did not create a materials handling business intent on serving large corporate customers and, at best, turning a blind eye to the single piece and low volume mailer.

And I quote, "The cost of establishing and maintaining the Postal Service shall not be apportioned to impair the overall value of such service to the people."

We believe that this cross-subsidization between classes has in fact been the norm and is a practice which continues to this day, as my colleague Mr. Weiss will demonstrate in his remarks.

The future must include a strong, well managed and financially stable Postal Service providing for frequent, universal and timely mail delivery at uniform, reasonable and fair rates.

Just as businesses have had to face the challenges of technology, competition, changing consumer behavior, and have reshaped and revitalized themselves to operate efficiently, so must our Nation's Postal Service.

As Mr. Mayer will propose, we believe that changing technology can be adopted for increasingly cost efficient mail delivery, and that that cost efficiency must extend to all mailers, not just a few. And we would expect to participate in any group of government and industry to make this a reality.

We believe that changing models for labor-management relations are necessary for businesses in the next century, and as individual companies, we are working to define these in a positive and productive manner.

We expect that some of these ideas will be relevant in defining the new labor management environment so essential to the effective functioning where over 80 percent of the cost structure is labor.

We believe that whatever the future of bulk mail and business-to-business communications, that there are compelling national, social, and humanitarian arguments for our Government's continued support, sponsorship and safeguarding of reasonable cost access to the mail system.

The mail system is not simply a business. It is a Government protected monopoly that binds the Nation together. It will require on-going regulatory and legislative involvement to ensure these very basic and these very important American public needs are met and protected.

Thank you very much.

[The prepared statement of Mr. Davison follows:]

PREPARED STATEMENT OF HAMILTON DAVISON

Good morning Mr. Chairman, distinguished Members of the Committee. My name is Hamilton Davison, president of the Greeting Card Association. I am also president and CEO of Paramount Cards in Pawtucket, Rhode Island. On my far right is Jeff Weiss, vice president of the Greeting Card Association and executive director—everyday cards product development with the American Greetings Corporation in Cleveland, Ohio. On my right is Jack Mayer, chairman of the Greeting Card Association's Postal Affairs Committee, and division vice president—strategic planning with Hallmark Cards, in Kansas City, Missouri.

Introduction

The greeting card industry in America represents nearly $7 billion in sales at retail each year and directly and indirectly employs over a quarter million Americans. Because more than two-thirds of all greeting cards are mailed, our future is inextricably bound together with the U.S. Postal Service (USPS). Our association has a long history of interaction with the Postal Service, dating back to World War II when, as the National Association of Greeting Card Publishers, we helped support the War Bond effort through the sale of "Defense Stamp Christmas Cards" and the sending of V-mail greeting cards. In more recent times, during Desert Storm/Desert Shield, we helped bolster troops overseas by contributing cards to school children so they could show their support of our troops. We have performed many collaborative promotions with the Postal Service. Beginning in 1943 and continuing through the 1980's we promoted an annual "Shop Early—Mail Early" campaign at Christmas-time. Last year, we participated in the USPS's national "Card and Letter Writing Week," and we are interested in actively promoting any initiative to increase the unit volume of mail. We have worked with the Postal Service to increase efficiency. Over the past several years our members voluntarily eliminated dark colored envelopes from the mail stream. Dark envelope colors hamper use of the automation technology. The Greeting Card Association (GCA) was recognized with the USPS's "Partners in Progress" award as a result. As an industry, both collectively and individually, postal matters received considerable attention—including such issues as the future of the U.S. Mail in the electronic information age, people's perception of the mail service, and possible solutions to the consumer's rising costs of postage.

However, we are before you today not simply to insure the well-being of a trade group. We are here advocating for the best interest of more than 250 million Americans who use the U.S. Mail to send correspondence and news to family and friends. By the very nature of our product, our vested interest puts us solidly in line with the best interests of the citizen mailer, who we sometimes refer to as "Aunt Minnie". As an industry, we have a history of advocacy for, and intervention on behalf of Aunt Minnie. In addition to a long-standing relationship with the Postal Service, the GCA has appeared before Members of Congress and has represented Aunt Minnie in the regulatory process. Our customers tell us first-class mail is the most important mail they receive each day and that part of the mail opened first by Americans after receiving their daily delivery.

The Postal Mandate

Americans have a deeply rooted sense of their Postal Service. Ask any American about postal matters and you are likely to get an earful of prescriptive suggestions and personal anecdotes. Americans have an individual relationship with their mail carrier, often wishing him or her well as they toil through "rain, sleet, snow" (particularly this year) making every effort to deliver to us our mail. We may not know in which federal tax bracket we belong but nearly every American knows it costs 32 cents to mail a card or letter. We are taught from childhood that first-class mail is specific to each person: you never open someone else's mail. In fact, focus groups conduced for our industry reveal that Americans believe electronic communications can be intercepted, but that first-class mail is private and secure. First-class mail has been characterized as important to people. The USPS's own household diary studies confirm this. What is the first thing we open when the mail comes? Except at tax refund time when we grab for a distinctive looking manila envelope, it is the valued personal correspondence from people dear to us that gets our first attention. Consumers tell us there are certain tasks that only a letter or card could perform. The Pony Express is still immortalized in our history and popular culture. Most every school age child knows Ben Franklin was our first Postmaster. Legal contracts reference serving notice through first-class mail. We communicate with each other through the mail and we communicate with our government through the mail. The post office is for many the quintessential governmental symbol, an institution deeply ingrained in our sense of culture and an important icon for the United States Government itself.

Going as far back as the Constitution of 1798, the U.S. Postal Service fulfills its congressional-mandated role as a provider of universal communication service "binding the Nation together through the . . . correspondence of the people." Congress knew that the letter mailer might be exploited, as when in 1970 you admonished the Postal Service not to load costs onto the user for which the USPS was given a monopoly. You established an independent Postal Rate Commission to continue the tradition of checks and balances so critical to the proper functioning of our democracy in a free market-economy. As you intended that the Postal Service serve the interests of the commonweal, you instructed it to be fair and equitable in setting rates, to consider the value of the service to the sender and recipient, to consider the availability of alternatives, to consider the educational, cultural, scientific or informational content of each piece of mail it handles, and to insure that one class of mail does not cross subsidize another. You created a monopoly in the public interest to serve the public when it communicates. You did not create a materials handling business intent on servicing large corporate customers and—at best—turning a blind eye to the single piece and low volume users. ". . . The costs of establishing and maintaining the Postal Service shall not be apportioned to impair the overall value of such service to the people." We believe that this cross subsidization has in fact been the norm, and is a practice which continues to this day, as my colleague Jeff Weiss will cover in his remarks.

Future Vision

We hope the future will include a strong, well-managed and financially stable Postal Service providing for frequent, universal and timely mail delivery at uniform, reasonable and fair rates. Just as businesses have had to face the challenges of technology, competition and changing consumer behavior, and have reshaped and revitalized themselves to operate efficiently, so must our Nation's postal service.

As Jack Mayer will discuss, we believe that changing technology can be adapted to provide for increasingly cost efficient mail delivery, for all mailers, not just a few, and we hope to participate with a consortium of government and industry to make this vision a reality.

We believe that changing models for labor-management relations are necessary for businesses in the next century and as individual companies we are working to

define these in a positive and productive manner. We hope that some of these ideas will be relevant in defining the new labor management environment so essential to the effective functioning of an entity more than 80 percent of the cost structure is labor.

We believe that, whatever the future fate of bulk mail and business to business communications, there are compelling national, social and humanitarian arguments for government's continued support, sponsorship, and safeguarding of American households to enjoy at a reasonable cost access to a mail system. The mail system is not simply a business. It is a government protected monopoly that binds the Nation together. As such, the USPS will require on-going regulatory and legislative involvement to ensure the very basic and very important needs of the American public are met and protected.

Thank you very much.

Senator SMITH. Mr. Weiss.

TESTIMONY OF JEFF WEISS, AMERICAN GREETINGS CORPORATION

Mr. WEISS. Good morning, Mr. Chairman and distinguished Members of the Committee.

My name is Jeff Weiss, vice president of the Greeting Card Association. I am also executive director of Product Management, Everyday Cards for American Greetings, headquartered in Cleveland, Ohio.

I thank you for the opportunity to present my testimony before you today. Before I begin, I'd like to request that the two appendices that I referred to be included in the record in their entirety.

Senator SMITH. Without objection.

Mr. WEISS. I am pleased to be here today to share with you our thoughts on the future of the Postal Service. Specifically, I'll be addressing two topics. First, the importance of the Postal Rate Commission, and second, the hazards of cross-subsidization.

In order to effectively explore the future of the Postal Service, it is essential that we understand the past, the history that binds us and brings us to this Senate Committee.

The greeting card industry and the Postal Service have a unique and special relationship. More than two-thirds of all greeting cards reach their intended recipient through the U.S. Postal Service.

Likewise, more than half of all household-to-household mail is comprised of greeting cards.

Thus, we are intertwined and it makes good sense for us to work together to jointly meet the needs of our very important customer, the citizen mailer.

For the reason I just mentioned, the Greeting Card Association speaks for the needs and perspectives of the citizen mailer.

Given this unique relationship, it has always been a key objective of the Greeting Card Association to support a strong and efficient Postal Service.

Our industry feels the Postal Rate Commission will be important in the future. The 1970 Postal Reorganization Act reaffirmed the mission of the U.S. Postal Service, namely, "To bind the Nation together through the personal, educational, literary and business correspondence of the people."

Additionally, the Postal Reorganization Act removed the process of rate setting from Congress and established the Postal Rate Com-

mission to review all rate changes and to ensure fair and equitable rates.

As you know, Congress established nine criteria which the Postal Rate Commission must follow in recommending new rates. These are listed in Appendix A.

Through the Postal Rate Commission, Congress removed itself from the process of setting postal rates and established checks and balances needed to set postal rates fairly and effectively. We believe it is essential to preserve the checks and balances that are currently in place in the rate setting process.

Without effective checks and balances, it would be all too easy for prices to fall in classes of mail where the Postal Service has competition, and prices to rise in classes where a monopoly exists.

In a speech on March 5, 1996 before the Postal Board of Governors, the Postmaster General identified some of his thoughts on the future vision of the Postal Service: "Last July, JCPenney signed a billion dollar deal with the competition. The head of their catalog division told me later that they would rather have given the business to the Postal Service. The problem was we did not have the freedom to meet their needs. I'm going to do everything I can to help us get the freedom to compete in the coming months."

We have grave concern that the pricing freedoms sought by the Postal Service will result in reduced contribution to institutional costs, thereby increasing the burden on first-class mail, particularly, citizens and small mailers.

If this "freedom" is defined as the elimination of valuable checks and balances in setting rates, such freedom is not in our vision of the future of the Postal Service. Any pricing initiative should be tested against the impact it will have on cost and prices of first-class mail and the citizen mailer, pursuant to the nine criteria I mentioned earlier.

Now let me talk about cross-subsidization. In testimony in a recent reclassification case, and summarized in the attached analysis, Appendix B, economist James Clifton provides evidence to illustrate how the current pricing of the U.S. Postal Service is causing a cross-subsidization of third-class mail through first-class rates.

We feel that any move to provide the U.S. Postal Service any more "market freedom" will only further perpetuate this cross-subsidization.

The unique provision of the private express statute and the resulting monopoly of first-class letter mail requires on-going oversight from a strong Postal Rate Commission. This is the only way to ensure fairness in setting first-class rates.

The Postmaster General further states in the same remarks on March 5, 1996 that: "Clearly the process takes too long, a delay that benefits neither household customers, the Nation's businesses, nor the Postal Service. We must continue to press forward for postal reform that will simply and streamline the rate setting process."

While it appears that the process is long and cumbersome, the reality is that the process of setting fair rates in accordance with the nine criteria established in the 1970 Postal Reorganization Act requires the process followed by the Postal Rate Commission today.

its related decision-making criteria . . . must be reconfirmed and used as a benchmark throughout your discussions of postal reform and any legislation that might be forthcoming.

The GCA recognizes that the Postal Service is facing a changing environment and potential threats to its current performance. Just as all businesses face the challenges of technology, competition and changing consumer behavior, and must reshape and revitalize themselves to operate effectively in the 21st century . . . so must the USPS.

The greeting card industry and the Postal Service have a proud, successful history of working together to serve the needs of the citizen mailer. We look forward to continuing that partnership and to working jointly to ensure a fair, efficient, effective postal system in the 21st century.

APPENDIX A

RATE MAKING CRITERIA

1. To be fair and equitable in setting rates.
2. To consider the value of service from the viewpoint of both the sender and the recipient.
3. To make sure that each class individually covers the costs which it causes, and therefore to avoid cross subsidization.
4. To look at the effect the rate change will have on the general public and competitors.
5. To consider the availability of alternatives to the Postal Service.
6. To take into account what is called work sharing or outside preparation by mailers.
7. To simplify whenever possible.
8. To acknowledge the acronym "ECSI" which stands for educational, cultural, scientific and informational content within a particular piece.
9. To use expertise and good judgment of the PRC in matters affecting rate designs which the commission deems appropriate.

APPENDIX B

The Longstanding Problem of Cross-Subsidization Between First- and Third-Class Would Only Be Worsened by USPS' Insistence on "Greater Pricing Flexibility."

While GCA does not agree with the recommendations made in a recent American Enterprise monograph, it does agree with the following findings made by the authors:

1. "The statutory monopoly over first-class mail delivery makes it relatively easy for the Postal service to engage in cross-subsidization of competitive activities (such as parcel post and overnight mail) and to pass the cost along to captive customers."
2. The Post Office's ratemaking procedures repeatedly produced cross-subsidies running from first-class mail to other mail services. In reaction to that practice, Congress in 1970 constrained the discretion of postal managers in setting rates for the classes of mail."
3. "In 1976 the Postal Service was taken to task for its ratemaking procedures by the U.S. Court of Appeals for the District of Columbia Circuit in *National Association of Greeting Card Publishers v. United States Postal Service* . . . On that basis, the court rejected the Postal Service's use of the inverse elasticity rule and agreed with the argument that the rule "preserved historical rate differentials and otherwise unduly and unreasonably discriminated against first-class mail."

Source: Sidak, J. and Spulber, D., *Protecting Competition from the Postal Monopoly,* (AEI Press, 1996), pp. 120–121.

The "inverse elasticity pricing rule" referred to above is also called Ramsey pricing and originally showed how a national tax monopolist could maximize tax revenue across different constituents. While the rule is applied today in regulatory and business circles to show how multi-product firms should price in the face of economies of scale or scope, the rule was not designed to show how an enterprise should price where it has a monopoly in one product and competes with other firms in the remainder of its products.

Ramsey pricing has, unfortunately, crept back into the rate making practices of the Postal Service and the Postal Rate Commission's adjudication of them. While

it was not the primary focus of his testimony in the recent reclassification case (MC95–1), GCA expert witness Dr. James A. Clifton did produce tables to his direct testimony showing how Ramsey pricing has crept back in.

TABLE 1

COMPARISON OF ALTERNATIVE APPROACHES TO SETTING RATES AND THE COMMISSION'S RECOMMENDED RATE FOR FIRST-CLASS LETTERS

	(Cents Per Piece)		
	R87–1	R90–1	R94–1
Alternatives			
USPS Proposal	25.0	30.0	32.0
Ramsey Based/IEP Prices	25.8	29.2	33.4
Uniform Markup on Attributable Cost	23.4	26.9	28.8
Commission Recommendation and Final Rate	25.0	29.0	32.0
Differences			
Commission minus Postal Service	0.0	(1 0)	0.0
Commission minus Uniform Markup	1.6	2.1	3.2

TABLE 2

COMPARISON OF ALTERNATIVE APPROACHES TO SETTING RATES AND THE COMMISSION'S RECOMMENDED RATE FOR BULK REGULAR CARRIER ROUTE PRESORTED LETTERS

	(Cents Per Piece)		
	R87–1	R90–1	R94–1
Alternatives			
USPS Proposal	10.1	12.3	14.4
Ramsey Based/IEP Prices	11.2	14.3	14.3
Uniform Markup on Attributable Cost	10.6	13.4	15.6
Commission Recommended and Final Rate	10.1	13.1	15.0
Differences			
Commission minus Postal Service	0.0	0.8	0.6
Commission minus Uniform Markup	(0.5)	(0.3)	(0.6)

Sources: Postal Rate commission, *Opinion and Recommended Decision,* R87–1, R90–1, R94–1. H.W. Beecher and A.S. Wawrukiewicz, *U.S. Domestic Postal Rates, 1872–1993.* United States Postal Service, *Postal Bulletin,* 1987–1994.

In 1987, 1990 and 1994, following the 1983 Supreme Court decision which gave the Postal Rate Commission ultimate discretion in interpreting the rate setting criteria of the 1970 postal reorganization act, the final rates set for First-Class letters have been close to Ramsey prices based on the inverse elasticity rule. By contrast, representative rates for third-class such as bulk regular carrier route presort have been set even lower than Ramsey prices. In some sense this suggests that the magnitude of the cross subsidy between first- and third-class produces a price for third-class mail that is below the price warranted by competitive conditions in that market, and the growing market share of the Postal Service for such mail is tentative evidence that the subsidized rates may border on being predatory. Indeed, in the 1994 rate case, expert witness John Haldi made claims of predation in Postal Service pricing practices.

The American Enterprise Institute and expert Dr. James A. Clifton are not the only ones to assert the current process produces cross subsidies. Dr. Robert W. Crandall, in direct testimony during MC95–1 on behalf of the Newspaper Association of America, pointed to the likelihood of cross subsidization under current postal rate making practices.

> "Second, the Postal Service is not regulated in the same manner as most public utilities. Although it must submit its rate and service-class proposals to the Postal Rate Commission, there are no mechanisms formally available to the Commission to insure against cross-subsidies. For example, my understanding is that, unlike federal and state regulatory commissions in most other sectors, the Commission cannot even compel the postal service to produce the data that the Commission would need to assure the public

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that competitive services are not being cross-subsidized by First-Class mail."

Source: Postal Rate Commission, Docket No. MC95–1, "Direct Testimony of Robert W. Crandall on behalf of the Newspaper Association of America", NAA–T–1, July 27, 1995, p. 5.

In the 1995 reclassification case, the Postal Service did win approval of its proposed new subclass for third-class carrier route presorted mail. Dr. Crandall and NAA rightfully opposed this proposal on the grounds that under current institutional arrangements it could lead to unfair competition and cross subsidies. (See Crandall, NAA–T–1, pp. 2–3)

The fundamental point made here is that legislation granting the Postal Service "greater pricing freedom" while further curtailing the powers of the Postal Rate Commission promises to escalate the level of unfair competition and cross-subsidization that already exists. It is bad for the general public, it is bad for efficiency, and it is bad for the future of the Postal Service.

Senator SMITH. Mr. Mayer.

TESTIMONY OF JACK MAYER, VICE PRESIDENT, STRATEGIC PLANNING, HALLMARK CARDS

Mr. MAYER. Thank you very much. Good morning, Mr. Chairman and Senator Smith. My name is Jack Mayer. I'm chairman of the Greeting Card Association Postal Subcommittee and division vice president, Hallmark Cards of Kansas City, Missouri.

Thank you for the opportunity to testify today on postal reform. In response to your invitation for this hearing, I will comment on our view of the future of the Postal Service and how that vision can become a reality.

The 21st century will be the information age. Information technology will transform our lives, what we do and how we do it.

The Postal Service must balance its traditional and legally mandated mission with the challenges and opportunities of the future.

We believe there will always be hard copy communications and the sending of tangible messages and items between people at different locations. The mix of activity most likely will change, but the need will not go away.

Radios and movies coexist with television, as someone alluded to earlier today. Bicycles coexist with automobiles. In this context, we offer our vision of the Postal Service 5 to 10 years from now.

In the future, the Postal Service must be efficient. Electronic technology will provide alternatives to postal consumers, and competition will seek to divert volume from the Postal Service.

In the 21st century the Postal Service must be a productive, efficient organization able to provide good value for its customers. The Postal Service of the year 2005 should strive to rank in the top quartile when benchmarked functionally against American industry.

In the future, the Postal Service must be growing. Nothing requires an organization to grow. However, it is difficult to stimulate people or to improve performance when growth is absent.

Growth represents a new challenge to the Postal Service since its heritage goes back before electricity, much less electronic communication.

The primary focus for the Postal Service should be on providing every encouragement for growth in all categories of its current

business. Improved service, appropriate consumer information, and new postal products can stimulate unit volume.

Additionally, new sources of growth related to the legislative mandate should be explored creatively but very carefully, since new businesses can be very costly, as Sears and IBM are finding out with Prodigy, for example. Not all electronics will make money.

In the future, the Postal Service must be technologically based. Information technology is rapidly becoming a core asset and a basic capability of leadership organizations.

In the 21st century, it will not be sufficient to automate yesterday's business processes. Technology provides the means to recreate ones' basic approach to business. The Postal Service of the future must be a willing and proficient participant in state-of-the-art technology.

In the future the Postal Service must be consumer friendly. Private express statutes require that the Postal Service balance the interests of individual users with those of larger mailers. The monopoly on first-class letter mail provides the umbrella for the Postal Service to serve those interests.

The successful organization of the future will understand its consumers' wants and needs and will excel at meeting them and exceeding them. The Postal Service must work to this end.

The four characteristics of the future I have described are frequently discussed in the business world, but rarely well executed. Focus, commitment and relentless pursuit are required for success.

We suggest some attributes the Postal Service must adopt to achieve these objectives. The Postal Service must be open, objective and creative as it thinks about its future. It must be receptive to new ideas and be willing to be change. Its size, heritage and focus on daily performance can inhibit new ideas.

Postal management must create an atmosphere where new thinking is encouraged and rewarded for all employees. However, new ideas bear no fruit if change does not occur.

All postal employees must be receptive to change. At the same time, employment security, retraining, and a caring environment are essential to encourage people to create and embrace change.

Success in the future will require new relationships between labor, management and customers. Some argue that the Postal Service has a large labor force, paid well above the private sector. Simply downsizing the Postal Service like AT&T is not a solution unless the workers affected are channeled into other gainful employment. New initiatives that break the antagonism of past labor-management relationships will be essential for future success.

The unique provisions of the private express statutes, and the resulting monopoly on first-class mail, require on-going oversight from a strong Postal Rate Commission to ensure fairness in the setting of first-class rates. The powerful gravity of large commercial mailers must be offset in order to guarantee fairness for those without such bargaining power and influence.

We must guard against proposals that will lead to no contribution to institutional costs from competitive classes, and, therefore, put all the burden for carrying the overhead costs on the monopoly class, namely first-class mail. The Postal Rate Commission provides those necessary checks and balances.

Now I'd like to offer two specific recommendations. First, the Postal Service should study how to bring the benefits of advanced technology to individual mailers. Many people work at home or out of their home, and many homes have personal computers and printers.

The economic benefits of technology and improved mail handling should be available to all. The Postal Service should initiate projects internally and with its outside partners to find ways for households and small mailers to utilize bar-coding technology and to receive the economic benefit therefrom.

Second, with technology diverting unit volume, postal management and postal labor have to work together to maintain an efficient, reasonably priced Postal Service. Handled carefully and thoughtfully, new business processes and new working relationships can lead to benefits for all.

It seems clear to us that the current antagonistic relationship between management and labor will not lead to success in the future. We strongly encourage a joint effort to review the entire situation and to recommend changes which will lead to major improvement in productivity.

In conclusion, consideration of postal reform is timely and important. It is better to anticipate and to prepare for change than to be its victim.

At the same time, it is essential that the public service aspects of the Postal Service be represented and that the Postal Service mandate to bind the Nation together be maintained.

We believe that the Postal Rate Commission has done its job well. In our view, the periodic disagreement between the Postal Rate Commission and the Postal Service reflects that the process is working.

As you look to the 21st century, we urge that the Postal Service execute its responsibilities within the current regulatory structure.

American households have no practical alternative for the delivery of their mail, nor do the member companies of the greeting card industry have an alternative for the delivery of their products. We rely on the Postal Service and have worked to support the Postal Service over the years. We will continue to do so, and we appreciate this opportunity to share our thoughts for the future.

Thank you.

[The prepared statement of Mr. Mayer follows:]

PREPARED STATEMENT OF JACK MAYER

Good morning, Mr. Chairman and distinguished Members of the Committee. My name is Jack Mayer, chairman of the GCA Postal Subcommittee and Division Vice-President—Strategic Planning of Hallmark Cards. I am pleased to be here today to discuss the challenging and exciting issue of postal reform.

Vision of the Future

The 21st century will be the information age. Information technology will transform our lives . . . what we do and how we do it. The Postal Service must balance its traditional and legally mandated mission with the challenges and opportunities of the future. We believe there will *always* be hard copy communication and the sending of tangible messages and items between people at different locations. The mix of activity most likely will change, but the need will not go away. Radios and movies co-exist with television. Bicycles coexist with automobiles. In this context we offer our view of the Postal Service 5 to 10 years from now. The Postal Service will be . . .

- *Efficient*—Electronic technology will provide alternatives to postal consumers and competition will seek to divert volume from the Postal Service. In the 21st century the USPS must be a productive, efficient organization able to provide good value to its customers. The USPS of 2005 should strive to rank in the top quartile when benchmarked functionally against American industry.
- *Growing*—Nothing requires an organization to grow. However, it is difficult to stimulate people or to improve performance when growth is absent. Growth represents a unique challenge for the USPS since its heritage goes back to the days before electricity, much less electronic communication. The primary focus for the USPS should be on providing every encouragement for growth in all categories of its current business. Improved service, appropriate consumer information, new postal products can stimulate unit volume. Additionally, new sources of growth related to the legislated mandate should be explored creatively, but carefully.
- *Technology-Based*—Information technology is rapidly becoming a core asset and a basic capability of leadership organizations. In the 21st century, it will not be sufficient to automate yesterday's business processes. Technology provides the means to recreate one's basic approach to business. The USPS of the future must be a willing and proficient participant in state-of-the-art technology.
- *Consumer Friendly*—The Private Express Statutes require that the Postal Service balance the interests of individual users with those of large mailers. The monopoly on first-class letter mail provides the umbrella for the USPS to serve those interests. The successful organization of the future will understand its consumers' wants and needs and will excel at meeting and exceeding them. The USPS must work to this end.

How The Vision Can Become a Reality

The four characteristics of the future vision described above are frequently discussed in the business world, but rarely well executed. Focus, commitment and relentless pursuit are required for success. We will suggest some approaches the USPS must adopt to achieve these objectives.

- *New Thinking*—The Postal Service must be open, objective and creative as it thinks about its future. It must be receptive to new ideas and be willing to change. Size, heritage and focus on daily performance can inhibit new ideas. Postal management must create an atmosphere where new thinking is encouraged and rewarded for all employees.
- *Change Orientation*—New ideas bear no fruit if change does not occur. All postal employees must be receptive to change. At the same time employment security, retraining and a caring environment are essential to encourage people to create and embrace change.
- *Cooperation*—Success in the future will require new relationships between labor, management and customers. Some argue that the USPS has an excessive labor force paid well above the private sector. Simply downsizing the Postal Service like AT&T is not a noble solution unless the workers affected are channeled into other gainful employment. New initiatives that break the antagonism of past labor/management relationships will be essential for future success.
- *Restraint*—The unique provisions of the Private Express Statutes and resulting monopoly on first-class letter mail require on-going oversight from a Strong Postal Rate Commission to ensure fairness in the setting of First-Class rates. The powerful gravity of large commercial mailers must be offset in order to guarantee fairness to those without such bargaining power and influence. The PRC provides those necessary checks and balances.

Specific Steps to Begin the Modernization Process Now

1. *Household Use of Bar Code Technology*—The Postal Service should study how to bring the benefits of advanced technology to individual mailers. Many people work at home or out of their home and many homes have PC's and printers. The economic benefit of technology and improved mail handling should be available to all. The USPS should initiate projects internally and with its outside partners to find ways for households and small mailers to utilize bar-coding technology.

2. *New Labor Management Environment*—With electronic technology diverting unit volume, postal management and postal labor have to work together to maintain an efficient, reasonably priced Postal Service. Handled carefully and thoughtfully, new business processes and new working relationships can lead to benefits for all. It seems clear to us that the current antagonistic relationship between management

and labor will not generate success in the future. We strongly encourage a joint effort to review the entire situation and to recommend changes which will lead to major improvement in productivity.

Concluding Remarks

Consideration of Postal reform is timely and important. It is better to anticipate and to prepare for change than to be its victim. At the same time, it is essential that the public service aspects of the Postal Service be represented and that the Postal Service's mandate to bind the Nation together be maintained. We believe that the Postal Rate Commission has done its job well. The periodic disagreement between the PRC and the USPS, in fact, reflects that the process is working. As you look to the 21st century, we urge that the Postal Service execute its responsibilities within the current regulatory structure.

The average American household has no practical alternative for the delivery of its mail, nor do the member companies of the greeting card industry have an alternative for delivery of their products. Our fate is inextricably linked. We rely on the Postal Service and have worked to support the USPS over the years. We will continue to do so and appreciate this opportunity to share our thoughts for the future.

Senator SMITH. I believe Mr. May is going to testify next.

TESTIMONY OF TIMOTHY J. MAY, GENERAL COUNSEL, THE PARCEL SHIPPERS ASSOCIATION; ACCOMPANIED BY M. JEROME JENSEN, JR., FINGERHUT COMPANIES, INC.; AND CHRIS REBELLO, CURRENT, INC.

Mr. MAY. Thank you, Chairman Stevens and Senator Smith. My name is Timothy May. I am the general counsel for The Parcel Shippers Association. The Parcel Shippers Association is a group of mail-order companies, many of them members, if not all of them, belong to the same associations that appeared here in the first panel.

They do business by sending out third-class advertising mail, both letters and catalogs, and some of them promote through first-class mail as well.

Their particular focus and concern, however, is the delivery of their product once the sale is made, and that is how that product will be delivered. It is delivered largely through either the United Parcel Service or the Postal Service, and that's why it is called the Parcel Shippers Association. That's their peculiar concern.

Accompanying me today on my immediate left is Jerome Jensen, Jr., who is with the Fingerhut Company, headquartered in Minneapolis, and next to him Chris Rebello of Current, Inc. in Colorado Springs, Colorado. Chris is the president of The Parcel Shippers Association, currently.

Let me say that our members are captive by several monopolies. When it comes to making their sales pitch through their mailing lists and their customers, they are largely captive of the postal monopoly over first and third-class letter mail.

The monopoly extends not just to first-class, Mr. Chairman, but it also covers third-class letter mail. And so in making their sales, they are covered by that monopoly.

In making their deliveries, they are largely captive to the biggest monopoly in the world for transportation, United Parcel Service. Only United Parcel Service and the Postal Service have a national delivery system for parcels to homes.

There is now some competition to United Parcel Service and the post office for what is called business-to-business delivery, Road-

way Express being the principal new kid on the block. And they are taking some business away from United Parcel Service.

The United Parcel Service has largely, over the years, focussed its efforts on trying to develop a volume business, and not necessarily huge, but they stop at my law firm, for example, where they come every day and they will pick up 15 or 20 parcels. That's the kind of business they want. They always target it, and that's what they get. They and only they and the post office deliver to homes.

So our members are captive to that monopoly and to the Postal Service monopoly. UPS gets the bulk of their parcel delivery business in part because they are able to cut deals. There has already been an allusion to a deal done a year ago between United Parcel Service and Penneys for a billion dollars in business. No one knows what the terms of that deal was, no one knows what price Penneys is paying for that.

UPS was perfectly free to sit down with Penneys and cut a deal. No regulatory agency had anything to say about it at all, even though they are in fact the largest de facto transportation monopoly in the world.

The Postal Service couldn't even begin to sit down and even have a discussion about what kind of a deal they might cut. That's wrong, and that's certainly one of the things we hope that this Committee can address, because there is no need to protect the public where there is that kind of competition. There is competition for the ground shipment of parcels between the post office and UPS, but unless the wraps are taken off, the Postal Service will never really be able to compete with UPS. And that's bad for the public.

There is a lot of competition in the expedited delivery market. There are a lot of competitors, Federal Express being very successful, United Parcel Service. I mean, there is a whole host of these expedited delivery companies, and you do not need a Postal Rate Commission with its arms wrapped around the post office in its attempt to compete in that market. The public and the marketplace will protect the public in that kind of shipment.

And in fact, Mr. Rebello, if asked, will tell you that they use a great deal of expedited delivery for their product. It depends on what your customer wants.

L.L.Bean testified today that they have shifted millions and millions of dollars of business to Federal Express. By the way, most of that came not from the post office, it came from UPS, I would guess. But their customers said they want that kind of fast treatment.

But the fact is that most of the business is shipped regularly through ground shipments and is not an expedited market, and that's controlled by these two companies, one of which can compete—UPS—and the other one can't because it is all tied up by the Postal Rate Commission regulations.

We hope that that is something that can be dealt with this year by this Committee.

Mr. Chairman, in announcing these, you said you hoped to make some first step toward modernization. You asked us to give you three steps that we could take this year, right now, to make things

better, to meet the vision that our members have for a post office 5 or 10 years from now.

I have to tell you that our members are worried about where we are going to be 5 or 10 years from now. And here are the reasons why.

The first one is the history over the last 8 years of congressional and administration raids on postal monies in order to help balance the budget. By 1998 that will be $14 billion of revenues our members have paid to the post office for service that will have been taken away from the post office and paid into the Federal treasury under the guise of redressing some past failures to pay under various pretexts, but in fact nothing other than a naked financial grab of this "cash cow," the Postal Service, which is off-budget, and taking that money and trying to help with the red ink in the Federal budget.

If the Postal Service were on-budget you wouldn't have taken a penny of that money away from the Postal Service. So that has got to stop.

Second, they are worried because they have perceived that some in Congress have been now saying that really we don't need a post office, it ought to be turned over to the private sector, that free enterprise can do this job, we don't need it any more. They are very worried about that kind of talk.

Even the most conservative of our members, who believe devoutly in the free market, do not see how we get from where we are now to this—how they get to the free market where ultimately somebody will come in and take up a void if you shut down the Postal Service. They fear that by that time they will be out of business.

They are extremely concerned over the complete failure of the Postal Service to reap the gains in productivity that should have been obtained from spending billions and billions of dollars on automation equipment.

The complement of people at the Postal Service is almost as large today as it was before they bought the first piece of automation equipment. In other words, all the productivity gains that should have been achieved through automation have simply not been realized.

They are extremely upset over what every witness has alluded to, and that is a deeply flawed labor-management relationship at the Postal Service.

Last, they are frustrated at what they see as the futility of waiting for the Postal Rate Commission to come into the 20th century and to actually apply some of the Postal Reorganization Act's mandates to get modern costing, modern pricing, and get modern economics into the Postal Service, and they hope that that can be alleviated.

They do not, however, as some suggest, want to shut down the Postal Rate Commission. They do not want to greatly sap its powers.

But they do want the Commission: (a) to start doing what they believe the law asked them to do all along, and (b) we do think there needs to be some changes in the way things are done at the Rate Commission because of the changed competitive environment.

Clearly, 25 years ago the post office didn't have any competition except for parcels. Twenty-five years ago UPS and the post office had exactly the same share of the parcel market, fourth-class parcel market, 50 percent of it.

That was before the Postal Rate Commission and United Parcel Service, participating at postal rate cases, drove up parcel post rates to the point where they practically put the post office out of the parcel post business.

Before the Postal Rate Commission got its hands on parcel post, UPS and the parcel post had exactly equal shares of the market.

We hope that whatever the congressional committees do, they do not damage what has been proven for 200 years to be something that works and the American people need, and that is the Postal Service that we think can last well into the middle of the next century, and then no one can tell you what the future of the Postal Service will be 50 years from now because no one can predict that future.

But certainly for the foreseeable business life of our companies, we see an indispensable role for the Postal Service. We don't want it sold off, we don't want it privatized, we don't want you to give away parts of the function. We need that system.

My two colleagues have asked me to use their time to finish my statement because they do not have a prepared statement to give but will be prepared to answer any questions that the Committee has or the staff has.

But if I may pursue this line for a few more minutes, Mr. Chairman, using their time.

So basically in the next 5 or 10 years we want the post office to continue to be what it has been, on several conditions. One, we want them to improve their efficiency. Two, we want them to invest more wisely in automation. Three, we want them freed from unnecessary regulatory constraints on their marketing and pricing. And we want them freed from political interference by the White House, by Congress, and by the Postal Rate Commission.

And by political interference, I don't mean Democrats or Republicans, I mean politics in the larger sense. And let me allude to an example of what I'm talking about, Mr. Chairman. In today's *Washington Post,* there is a lengthy story featuring testimony given yesterday by the Postmaster General and the Chairman of the Postal Rate Commission before Chairman McHugh's Committee on the House side.

The Chairman of the Postal Rate Commission, devoted, according to the newspaper account, his entire time, or at least that's all the papers reported, to attacking the Postal Service for in effect a bait and switch, misleading the public by claiming that it was going to pass on the benefits of automation to all American postal patrons, and that by rejecting the Commission's proposal for a deeply discounted bar coded reply envelope, that the governors of the Postal Service had broken faith with that commitment.

That is sheer demagoguery. It is engaging in politics. it is not helpful in the fractious relationship between the Postal Rate Commission and the Postal Service. In fact, in it is a completely misleading statement about what that particular proposal was.

The greeting card people here would not get any benefit at all from that. They don't use pre-printed bar code or reply envelopes. Now, we have all gotten these bar coded reply envelopes included in mail we get trying to sell us something, send back a card and it has the bar code on it.

And the proposal was that there would be a 12-cent discount on those envelopes. That 12 cents could have cost almost $800 million in revenue to the Postal Service.

And I have to tell you frankly, on behalf of this client and others, I opposed that proposal. I asked the principal witness supporting that proposal what the consequences would be to first-class mail. And he told me, under oath, that first-class mail should be raised one cent now in order to pay for this proposal.

Now, this is the proponent of this proposal. This is the same proposal that the Chairman of the Rate Commission yesterday attacked the Postal Service on, claiming that they had broken faith with the public by not going along with his hairbrained proposals.

Second, the principal beneficiaries of that proposal would be a few very large companies who send out business reply mail where the sender of the mail pays the postage and the consumer does not.

You may see in some of those return envelopes you have, it says business reply. When you use that and you send it back to American Express, for example, who is getting millions and millions of these, they pay the postage. They are the ones who are going to get that 12-cent discount.

So you had a proposal where hundreds of millions of dollars were going to be put into the pockets of very large companies. The governors properly rejected this, but we now have the Chairman of the Rate Commission denouncing the post office at a public hearing picked up in the papers, leading the American people to believe that once again the American people have gotten the short end of stick and that the Postal Service has taken sides with the large companies.

That is not helpful and that is not what Postal Rate Commissioners are supposed to be doing. They are supposed to be performing a judicial role.

Last, you asked me what things can we do right now to help?

No. 1, if Congress will only stop taking money away from the post office to balance the budget.

No. 2, there are on-going discussions in the post office and the Commission right now over procedural changes that don't require legislation that would improve things a great deal. The Commission looks like they are going to embrace some of them, but there are very important other proposals that indeed the Commission should seriously look at and everybody should get behind.

No. 3, we believe, Mr. Chairman, that your Committee should pass legislation that immediately, right now, deregulates parcel post and express mail from any Postal Rate Commission oversight with this exception. The Commission should be empowered to determine that the Postal Service is not causing a cross-subsidy to their competitive markets.

In other words, the Commission should be permitted to determine that whatever prices the Postal Service gets, negotiates,

charges, do cover the cost of that service. And, that the public gets the same deal, that everybody is treated equally.

If company "X" gets a really good deal from the post office, then company "Y," if it is willing to meet the same circumstance should also get the same deal. We believe that is a role for the Commission. But otherwise, they should have nothing to do with saying what the prices, conditions and classification are for parcel post and express mail.

No. 4, we think that indeed there has to be some discipline in the labor-management situation in the Postal Service. And we think that has to start with management. We haven't heard of anybody being fired at top management.

We read again and again how massive blunders made at the Postal Service, nobody gets disciplined, nobody gets fired. They get moved around. This is infectious. Why should the rank and file believe they should be disciplined if they don't see anything going on up top.

So that has to change, we think. And we also think there has to be a system of rewards, too. It can't be all one way. The postal management is handicapped now in being able to properly reward outstanding performance, and the rank and file have to be given incentives when they perform better. And that's too hierarchical and rigid a structure now that doesn't really allow for that. But I think they can come to that themselves if they were willing to do that.

Chairman STEVENS. Mr. May, I'm going to have to cut you off. We have another panel coming.

Mr. MAY. Yes, I am through, Mr. Chairman. Thank you.

[The prepared statement of Mr. May follows:]

PREPARED STATEMENT OF TIMOTHY J. MAY

My name is Timothy J. May. I am general counsel of The Parcel Shippers Association, a group of approximately 200 businesses which utilize the United State Postal Service and other carriers to ship parcels in interstate commerce. Our members are heavily reliant upon the Postal Service as the principal means for soliciting their customers through third class mailings; and these customers in turn use the Postal Service to place orders for merchandise, and to pay for that merchandise. Accompanying me today are Chris Rebello, the president of The Parcel Shippers Association, and director of Postal Affairs for Current, Inc., a large mail order company headquartered in Colorado Springs, Colorado; and M. Jerome Jensen, Jr., of the Fingerhut Companies, Inc., headquartered in Minneapolis.

Mr. Chairman we are aware of your announced intention, stated at the first round of hearings you conducted, that you were interested in going forward "by mid-year with legislation to take the first step toward modernization." Admonished by that, in our testimony today we will try to assist you and your colleagues in formulating proposals that would lead to that first step. Also, in calling for these hearings, you have asked us to concentrate on very practical suggestions about making things better, with focus on the following:

1. What is the vision of our members about the Postal Service 5 years from now and 10 years from now; in other words, what do we hope that the Postal Service can be, that it presumably is not now, 5 years from now and 10 years from now, and how can the Congress and the Postal Service and we who use it help our vision become a reality?
2. And recognizing that great reforms can take a long time and are, therefore, rarely achieved, you have asked us to come up with three specific steps that ought to be taken this year in order to start this modernization process. We hope we are able to give you very concrete answers. You have also asked that we try to express to you how the members of our industry feel about the future of the Post Office.

In a general response to these requests let me comment, first of all, about how our members feel about the future of the Post Office. They are very worried about its future. Part of that concern derives from the fact that they are so utterly dependent upon the Postal Service as the principal vehicle by which they maintain their business life. They do not quite know what they would do if there were not a Postal Service as it has been for more than two centuries. The business that most of our members are in is a business that could not ever have even come into existence without the indispensable presence of the Postal Service and its predecessors.

Our members' worry about the future is premised on a number of factors to which I will generally advert:

a. A continuing raid by Democratic and Republican Administrations alike, both the Executive Branch and the Congress, to try to milk the Postal Service "cash cow" as a way of alleviating some of the federal budget red ink;
b. A developing belief by some in the Congress that government should not be performing business functions and the Postal Service is fundamentally a business function;
c. The inexplicable failure of successive postal managements to increase real productivity in the Postal Service and to reduce the labor quotient of the production equation, notwithstanding the billions of dollars spent on automation which should have made obsolete large amounts of hand and mechanized postal labor;
d. A labor management-relationship which is deeply flawed. This may more fundamentally be the fault of the Postal Reorganization Act itself in creating a system where neither side will take a risk and where both sides have been led to believe, by the history of their negotiations, that they are best protected by letting arbitrators (who have little understanding of the postal system) decide what basic pay and working conditions will be.
e. Lastly, our members are dismayed about the futility of the Postal Rate Commission's handling of the rate and classification issues that ultimately determine the prices they pay, and the inherent inefficiencies that are perpetuated by the decades-long refusal of the Postal Rate Commission to honor the intentions of the Postal Reorganization Act to bring about modern pricing, costing, and classifications, as the fundamental lynch pins of modern postal economics.

What perhaps our members fear most are the unlearned political and ideological voices demanding the destruction of the Postal Service, with the absolute certitude they seem to have that the market will be a perfectly reliable supplier to fill the Postal Service void. while many of our more conservative members yield to no one in their convictions about the correctness and rigor of the free market, they are not convinced that the rescue by the marketplace would come in any real time sufficient to keep them in business by filling the void created. Thus, they worry when they hear powerful members and leaders in Congress, and others, say that they will get this done on their watch.

This fear conditions our members' visions and hopes of what the Postal Service will be 5 and 10 years from now. Most fundamentally they hope that it is there; that it has not been displaced or so wounded by selling off parts of the system and giving it away to private enterprise, or so opening the system to competition that the Postal Service as a national, universal carrier offering certainty of delivery at affordable prices is a thing of the past.

Our members would like the Committee to understand that they think the Postal Service is pretty good, so that their future vision largely is built around a Postal Service that is fundamentally doing what is done today with the following caveats:

—that it improves its efficiency and productivity;
—that it designs in ways to maximize the amount of production it gets from an intelligent labor force that has been given incentives to perform at the highest level;
—that it has wisely invested in the most efficient automation that will produce through-puts at the least possible cost and eliminate feather bedding;
—that it will have been freed from unnecessary constraints on its marketing and pricing to non-monopoly markets so that it can meet competition and behave like a rational, modernized business would towards its customers; and, frankly,
—that it is free, to the maximum extent possible, from political interference with the operation of what is essentially a business and not a policy operation. By that we mean that we hope that it will be free from political

interference by Congress, the White House, and the Postal Rate Commission.

We want the Postal Rate Commission to divorce itself from political views about its job, and focus solely on its core functions of determining costs of service and applying rational, congressionally mandated policies for allocating the overhead, without worrying about the political consequences of its decisions. The PRC was never intended to be a politically motivated body, despite the fact that those appointed to it are often appointed for political reasons. One must recall that a main purpose of the creation of the Postal Rate Commission was to get it out of the political log rolling that had characterized the fixing of postal rates by Congress for two centuries.

How do we get where we want to go? You have appropriately asked us to respond to that question and to give you three things that can actually be done this year that will speed the Postal Service on its way. We will try to suggest more than three:

1. Stop once and for all Congressional raids on the postal treasury under various pretexts that this is some form of balancing for past failures to pay;
2. The appropriate Congressional Committees should urge both postal management and the Postal Rate Commission to get together and adopt procedural reforms they are considering right now that will produce efficiencies in the way that rates and classifications and new product offerings are considered;
3. Legislatively deregulate certain non-monopoly services now;
4. The PMG should discipline those responsible for fiascoes that have cost the Service substantial amounts of money, loss of credibility, and public embarrassment. The perception that there is no public accountability at the Postal Service is compounded by the fact that those who commit massive blunders in full public view are never made to pay the price that most in the private sector would have to pay, including loss of their jobs. How can one expect the rank and file to give their best and, by peer pressure, enforce performance among their own widen they are daily affronted by the fact that egregiously bad decisions at top postal management levels are swept under the rug as though no one knew who was really responsible for such things as the cancellation of the Postal Buddy contract.
5. And when postal management gets its own house in order by putting some discipline into the system (and by discipline we mean a system of rewards and punishments, i.e., somebody loses their job for major blunders), then we believe that labor must put its house in order. We have a system where there is no meaningful discipline or ability to discipline the rank and file; where there are an absurdly high number of arbitration procedures for every conceivable labor management grievance; and where, to quote Vince Palladino, President of the Postal Supervisors, the most obvious reward that truly good supervisors are given for outstanding performance is more work, with protection for those who are not carrying their share. It is manifest that the labor management system is broke so we do not have to be concerned about the admonishment: "If it isn't broke, don't fix it!" It is terribly "broke." (On another day we could elaborate on the complicated ways in which a system can be designed and implemented that will cause great pain to both management and labor for their failure to reach reasonable accommodations.)

We should not continue the present situation where neither labor nor management pays any price for failing to bargain responsibly. Management gets off the hook because an independent arbitrator makes the award; the same is true for the labor leaders, who do not have to defend a decision they made in collective bargaining when they run for re-election. They simply point the finger of blame at an arbitrator for an unpopular result. It is ludicrous that the decision about how to spend some $40 billion is turned over to an independent group of arbitrators who bear no responsibility, and who will never be answerable in the future to those affected by their decision.

Mr. Chairman, we will elaborate now on some of the issues which we touched on, and others which will greatly influence the postal future.

I. The Dysfunctional Labor-Management Relationship.

As we have said we do not think that the labor management relationship is healthy nor do we think it has been for a long time. Some, including the Postmaster General, have hinted at getting rid of the Merit Systems Protection Board, Veterans Preference Rights, and numerous other rules and regulations that are believed to interfere with the ability of management to deal with the vast postal work force. Frankly, we doubt that solutions that radical are likely to be embraced. And yet, it seems obvious that change in the labor management structure must be made and

may offer the most significant opportunity for the Postal Service to improve its costs and its productivity and consequently its competitiveness, in the far more difficult world which it will face in the future. We do not believe collective bargaining is going to be displaced either. However, the Postmaster General and other critics of the system are absolutely correct when they condemn the current system of arbitrated settlements. It is the worst possible outcome to have these decisions imposed from the outside and be the choice and decision of neither management nor labor. In our society, when organized labor and management fail to reach agreement normally the result can be a strike or the threat of a strike. It is our sense that neither the Postal Service nor our members, nor the public, are willing to endure a postal strike. Thus, what are the alternatives to arbitration and strikes? Answers do not come easily, but those answers must be found.

One needs also to ask whether labor is willing to exchange the current lock step compensation system and rigid hierarchical structures that have characterized the Postal Service for all of this century for a more open and democratically organized structure where pay is tied in part to performance? Vincent Palladino, the President of the National Association of Postal Supervisors, has stated that his organization "remains open to pay for performance proposals." He stated further: "There is no question that the collective bargaining agreements since 1971 have gradually eroded our ability to manage the workroom floor. . . ." He added that: "A parallel problem is our inability to award our best performers, other than by just giving them more work, usually the work that should have been done by the poor performers."

The much ballyhooed restructuring of 3 years ago appears now to have been a bit of a sham in that its ostensible goal was to materially reduce the number of postal employees who, evidently, were believed to be not needed. After an initial shrinkage of some 50,000 employees the Postal Service has now worked its way back up, more than replacing all of those employees who left, to reach a new employment peak. Yet, the restructuring was not a total failure. Because of the restructuring everyone at the Postal Service at a managerial or supervisory level was forced to reexamine the work that they were doing and their relationship to the Postal Service and other units within the bureaucracy. Job titles were changed; responsibilities were reassigned; people were shifted to different jobs; everyone was forced to take a hard look at what they were doing. Some layers of the bureaucracy were peeled away, apparently for good, and there does seem to be a more directed work force that, from top to bottom, takes more seriously the oft cited statement that customers are the Service's first concern. And we think we have seen the beginnings of a less rigid hierarchical and authoritarian culture. However, until this puzzle is solved the billions and billions of dollars invested in automation will never achieve the intended return.

II. Reform of Postal Rate Making and Classification Reform of Postal Rate Making and Classification.

The Postal Rate Commission has proven itself a reluctant partner in the efforts made by the Postal Service and its customers to modernize. It has repeatedly demonstrated its unwillingness to allow the Postal Service to price its products as a modern business would. Most recently, its response to the Postal Service's attempt to achieve classification reform was an almost universal rejection of the proposals. It is true that the Commission refined a number of the rates to effectuate some rate reductions for highly automated mail, with consequent rate increases for the more costly to handle mail, and this greatly pleased most of our members as well as the mail order industry generally. However, while doing this the Commission also rejected every single attempt to reform the subclasses (with one minor exception), signaling a policy view that seems to suggest that any fundamental classification reform is forever doomed so long as the current Commission and staff are making policy and decisions.

The current Postmaster General, as did many of his predecessors, has argued that the Postal Rate Commission's powers must be severely reduced and the Postal Service given far more flexibility in setting rates and products. Naturally, we all prefer to have no one looking over our shoulder and monitoring what we are doing. However, we think that we need a Postal Rate Commission to make sure there is an honest game. On the other hand, we think that the various PMGs had a valid complaint that it simply takes too long to introduce a new postal product to the market. By the time the Postal Service gets through the maze of Rate Commission approval, which is rare, and gets its product to market, its competitors have already been there and own the new business. Much has been said about the Postal Service monopoly, but it needs to be remembered that a great deal of what is handled by the Postal Service is not protected by the monopoly. It is subject to both direct and indirect competition in the communications and delivery markets. The unwieldy and in-

ordinately time consuming process employed by the PRC that is now preventing the Postal Service from quickly introducing new and competitive products will ultimately doom that part of the Service's operations, thereby greatly eroding the support of its core business (the delivery of hard copy letter mail, both first- and third-class).

The Postal Service has to be given the tools to react far more rapidly to market conditions. It is PSA's position that the Commission should have no role in the approval of new products that are designed to meet existing competition where the Postal Service enjoys no monopoly. In such cases the public is more than adequately protected by competition; the public does not need the heavy hand of PRC regulation preventing a quick response to competitors or, as is more often the case, refusal to allow the Postal Service any response at all by rejection of Postal Service innovations. PSA does believe that the Commission has a role but that role should be solely to ensure that these new products are not cross-subsidized by monopoly services, and that these new products are available to all customers under equal circumstances. We believe that requires a change in the law and we see no reason why Congress can not get that done this year. We will go further to say that the Postal Service should be able on its own to establish the rates and condition of services for any of its existing products that are not subject to the postal monopoly, and where there is adequate private competition to ensure that the Postal Service does not abuse the public. The most obvious cases are Parcel Post and Express Mail.

A glaring failure of the Postal Reorganization Act has been its use by United Parcel Service and the Commission to practically destroy Parcel Post service. When the Postal Reorganization Act was passed, UPS and the Postal Service had an equal volume of fourth-class parcels. United Parcel Service is now the largest *de facto* monopoly in the free world. By constant participation at the maximum level in every single rate case, UPS persuaded the Postal Rate Commission to inflate the rates for parcel post, thereby allowing for higher UPS rates. The last several PRC rate actions on Parcel Post have attempted to reverse that trend and have indeed recognized the absolute essentiality of preserving Parcel Post as the only competition to UPS. That has helped, and Parcel Post has regained some small market share. We hope that the damage already done is not so permanent that Parcel Post can not be a significant market factor in the parcel delivery business; the public needs Parcel Post to be a serious competitor to the UPS giant.

In terms of things that can be done right now, we believe that it is within the power of the Commission, working with the Postal Service and its customers, to adopt a number of procedural changes which would greatly facilitate the rate and classification process, and eliminate time and expense from that process, while still preserving fundamental substantive and procedural rights. Many of these improvements are contained in proposals advanced by a Joint Task Force that produced proposals in the early nineties. At the Postal Service's request the Commission has reconsidered many of these proposals, and has now issued proposed amendments of the rules of practice and procedure that embody a number of these recommendations. These proposed amendments will provide for expedited review to allow market tests; expedited review of requests for provisional service changes; and the use of multi-year test years for new services. These amendments would also allow for expedited consideration of minor classification changes. We hope very much that the Commission will finalize these proposed changes. At the same time we are disappointed that the Commission failed to act on several other very important proposals that have been pending before it. We believe that it is crucial that the Commission adopt procedures that allow rate bands for competitive services and allow for negotiated service contracts so that the Postal Service can at least have a chance to meet competition. Of course, as we have elsewhere testified, we do not believe that the Commission should be doing any of this in the case of Parcel Post, which we think should be completely deregulated with its rates and services determined by the marketplace.

III. The Postal Monopoly and Privatization.

Let me briefly address the related topics of the continuance of the postal monopoly and privatization of postal functions. For many years there have been critics of the postal monopoly although most of us did not take them seriously. It is not surprising that this is being looked at anew. At a time when every government agency is being scrutinized to determine whether that agency and its mission remain essential to the public, it is to be expected there would be a reexamination of the continuation of the postal monopoly and/or the privatization of all or part of the Postal Service.

We think the Postal Service issue can be distinguished from the discussion about the essentiality of other government agencies and functions performed by them. While many of these governmental functions have been disparaged as something

that does not need to be done by anyone let alone the government, at least what the Postal Service is doing now is essential for this country and is certainly essential for the industry to which our members belong. Thus, the question really is who should perform those functions: a quasi-government agency like the Postal Service, or the private sector, or a partnership between the two. An aspect of this issue is whether it is really possible ever to have an efficient Postal Service so long as it has the protection of the postal monopoly. An additional corollary is that so long as there is a monopoly, there will have to be a Rate Commission, either this one or some differently constituted one that regulates that monopoly in terms of the prices and services it offers in order to ensure they are fair and equitable to the public. Thus, some among the postal community who would abolish the monopoly would abolish it as a way of getting rid of the Rate Commission.

Last year the Mailers Council had a survey taken the results of which suggest that 70 pecent of Americans believe that the quality of the service provided by the Post Office would improve if private companies were allowed to compete for the delivery of postal products. As I have said before, I am only surprised that as many as 30 pecent believe service would not be improved if there were competition. After all, one would not expect the American people to understand the very complicated issues of the dependence of universal postal service upon a monopoly and the possible financial devastation to mail left behind still captive to the Postal Service because the private companies simply do not want to deliver it. Yet, this Committee and all other knowledgeable parties can be expected to responsibly understand the interconnectedness of those issues and not engage in demagoguery about the postal monopoly versus the virtues of the free market.

Certainly a problem that all users of the Post Office have is that, to the extent that they are being provided a monopoly service, since there is no competing service with which to compare, they do not know how good or efficient that service is. On the other hand, in terms of parcel deliveries for our members, we do have a very good basis to compare service and price because there is competition.

I can tell you that so far as the prices they pay for their third-class advertising messages, our members do not think that the service they are getting and the price they are paying are fair, and they do not blame the Postal Service for that. They are well aware that the Postal Service has asked for lower prices for third-class products in the last three rate cases, and in the last classification case, and that four times in a row the Postal Rate Commission has raised third-class rates higher than the Postal Service asked for. My members also know as a fact that managers can not get the most out of their employee work force when a company is not faced with competition and thus the possibility that the employees will lose their jobs if business is lost. Because the Post Office has never suffered a decline in volume or revenues in more than 25 years, in all of that time no postal employee has lost a job due to the fact that business or revenues have been lost. That we can assure you would never be replicated in the private sector.

I can not tell you today that all of our members are completely comfortable with the postal monopoly; in fact, many of them have a lot of questions about its continued value. On the other hand, I can assure you that they are gravely concerned about the possibility of serious disruption and damage that could result if the monopoly is eliminated. For that reason, as a group they do not want any reckless actions taken; they do not want a change in the postal monopoly until there is a full understanding of the consequences; and a willingness by those who use the Post Office to live with those consequences. I know that this Committee has asked the GAO to measure the effects of the continuation or the elimination of the postal monopoly and we eagerly await the results of that study which we understand are imminent.

IV. The Advent of the Electronic Age.

In the short run PSA members want to ensure that the Postal Service is able to deliver hard copy messages at an affordable cost, and in a reliable and timely manner, and that it remains able to utilize its carrier delivery force to capture a significant share of the parcel delivery market, a market where many of our members are far too dependent on United Parcel Service (a company that truly does enjoy a monopoly in the home delivery of parcels). Most of our members reach their customers by mailing hard copy letters or catalogs to businesses and American households; receiving orders back from those customers, usually by mail, and then arranging for the products they have sold to be delivered, more often by United Parcel Service and to a lesser extent by Parcel Post delivery.

The evolution of the interactive electronic media market casts a large shadow over this traditional way of doing business. While the Direct Marketing Association estimate of the amount of consumer products and services that were sold by electronic media was less than $3 billion in 1995, that same DMA survey reported that 10

years from now the survey correspondents expected that market to exceed $28 billion. That necessarily means that a lot of direct mail and catalogs are not going to be sent to make those sales; also a lot of responses won't be using the mail. It is probably simply a matter of time before the public, probably our children and theirs, become quite accustomed to selling and buying through electronic media. As that happens the less important it will be to have the ability to deliver hard copy messages. This may mean that the Postal Service will at some point find itself out of date; but that could be equally true for many of our members. They also will have to adapt and change or they will find themselves out of date. However, we do not see that occurring for some period of time into the next century. Moreover, however products may be sold in that long-term future, the products themselves are going to have to be delivered. In other words, the merchandise, the book, the record, has to be transported to the purchaser. And that is where there will always be an opportunity for the Postal Service to marry its unmatched capability to deliver to every home in America, probably in partnership with a variety of other kinds of transportation companies that will bring products to delivery points where they are tendered to the Postal Service for home and business delivery.

V. Conclusion

While Postal users and the Congress are now taking a look at legislative change, we should take a while to reflect on just how successful postal reform has actually been. When postal reform was enacted over 25 years ago, the old Post Office Department was in far greater crisis than it is today. It was encumbered by a host of laws and regulations that incapacitated it from operating efficiently, and saddled with a rate-making system administered by the Congress itself. Furthermore, Congress subsidized postal operations by an average of twenty-five percent (25%) of total costs. In today's numbers that would be the equivalent of a subsidy to the Postal Service from the Treasury of $14 billion a year. With the passage of the Act, the Postal Service's dependence upon Congressional appropriations was phased out and finally ended, forcing the Postal Service to live off the revenues generated from the services it performed for the American people. The taxpayers today pay nothing for the service they receive. Based on where the Postal Service came from at that time, fairly judged the Postal Service must be pronounced a success. Its labor management relations are certainly less than ideal, but wages and working conditions are negotiated in a fairer way today; postal rates and classes are established in a more scientific and rational method.

At the same time, however, the Postal Service could be facing its most serious test in two centuries. It may be the case that 25 years ago it was not that essential to ensure that the Postal Service was highly efficient because most of what the Postal Service did was unique; there was no competition. For example, at that time there would have been no reason why the Postal Rate Commission could not take a year to get new prices in place or new classes or subclasses established, or to review whether or not USPS should be allowed to bring a new product to the market. Because the Postal Service did not by and large have to meet competitors in the marketplace there was no great rush needed to review these things. That day is over.

The Postal Reorganization Act dealt very well with circumstances existing at the time of its enactment, but it was established to deal with a market place quite different than that which the Postal Service faces today—one of increasing competition to deliver the essential communications that for centuries had been the exclusive preserve of the Postal Service. While Postal Service volume continues to grow, it is a fact that the Postal Service has lost an ever increasing share of the message market to alternative communication media. One can look down the road not too far and see a day when the Postal Service's share of the message market has so declined that there will actually be a real decline in first-class volume. That trend is probably irreversible because of technology. However, the Postal Service needs to be as efficient as it possibly can; it needs to offer the best kind of product it can in order to prolong that day. It must capitalize on its natural strengths, its principal asset being its unique delivery system which reaches every home and business 6 days a week. What the Postal Service has proven time and again is that the one thing it has never been able to handle is a decline in volume. It is incapable of downsizing, in part because it is so labor intensive.

Today we have discussed many of the faults of the Postal Service; faults in the way we believe the Postal Rate Commission does its job; our complaints about the raids that successive Administrations and Congresses have made upon postal revenues for extraneous reasons. And we have certainly told you our fears for the future. Despite all that, we do hope that the Committee will bear in mind, while they consider the Postal Service's future, that the Postal Service remains an indispensable communication link for all of our members as well as a large segment of the postal

community. Over $29 billion was invested by American business in marketing through the United States Postal Service in 1994. That equals television and newspapers for the American advertising dollar. And that was a pretty good investment because that $29 billion that was spent with the Postal Service paid off when customers bought more than $200 billion mail order purchases in 1994. I would expect that when the final numbers are in 1995 will be even more impressive.

You have asked what we see 5 years from now and 10 years from now for the Postal Service. We must tell you frankly that in the next 10 years it is simply not going to be possible for our members as well as most other mail order companies and publishers to find any substitute for the current type of hard copy communication that is available exclusively from the Postal Service. However, that service must remain affordable if it is to retain its value. It concerns us greatly to learn from the Postmaster General that the Post Office's share of the financial transaction market place declined 35 pecent and that he has predicted another 35 pecent loss in market share by the year 2000. The loss of that kind of volume and revenue, almost all first-class mail, when coupled with the pressures from outside, such as Congressional raids on postal revenues that will accumulate to $14 billion by 1998, are going to force higher postal prices. The Postal Service in the future is simply too fragile to be able to afford to subsidize the Treasury and taxpayers by paying over postal revenues to help balance the budget.

As we have told your House counterparts, a new era is upon us with new leadership in the Congress. We like to think that we and this Committee start with a fresh slate. We have to say that in the past we have often felt the Congress has more often been the enemy rather than the friend of the Postal Service. While pointing the accusing finger at an inefficient Post Office with one hand for the last decade the Congress with the other hand has reached into the postal treasury and looted it of billions of dollars. It is not an exaggeration to say that many of the financial and operational crises and the service deterioration in the Postal Service over recent years can be traced directly to the loss of those revenues. With new Congressional leadership we are encouraged to believe that can be put in the past and that we can look forward to genuine interest and concern by the Congress in the preservation of this national resource, the nation's universal delivery system upon which all of its citizens depend and which is the indispensable tool of the mail order industry.

Chairman STEVENS. It shows the advantage of having statements before we create the panels, because this is sort of a diverse panel.

Do you have some questions, Mr. Smith?

Senator SMITH. Just a couple, Mr. Chairman.

Mr. May, I was kind of taken aback by some of your comments, which I think some would view as being confrontational, but it is interesting that you take those positions. With the union situation, there is always somebody that is expendable at the management level, but there is never anybody expendable at the employee level. You can't get rid of anybody at that level, but there are always people available we can shuffle off somewhere in the management level.

I mean, is there ever anybody at the union level that could be let go because they are not doing their job?

Mr. MAY. In fact, Senator, what happened 3 years ago in the much ballyhooed restructuring, 50,000 people left the Postal Service, and the bulk of them indeed were the rank and file who took the early retirement. The next thing the service went down the chute, everybody is on overtime, and now those 50,000 people are back on the payroll. In fact, they have now exceeded that complement. So much for that. They did try to see if they could get by with fewer people.

Senator SMITH. Just give me two or three specific examples of this "cash cow" situation where we are raiding the post office to balance the budget.

Mr. MAY. Well, three times and over the Congress has claimed the Postal Service has not paid its appropriate share of its employees for the health and benefits for annuitants. That's an example.

Under various guises, the Congress also cut off the amount that they originally were supposed to be paying for nonprofit mail so that the rest of the mailers are now in effect subsidizing a significant part of the overhead cost of nonprofit mail. Just by the stroke of a pen that burden was imposed on the mailers. That was again contrary to what the intentions of the Postal Reorganization Act were. There are other examples.

Senator SMITH. If the intention is to balance the budget, I would agree we probably ought to stop it because we are not getting the budget balanced, so that doesn't seem to be working very well.

Mr. Davison, I just want to ask you one question, and that's all I have, Mr. Chairman.

It might not have been you. It was one of your panel there that talked about the fact that there would be not a diminishing situation but more use of mail, more dependence upon the Postal Service in terms of greeting cards.

What about the E–Mail situation though, where greetings are being sent via the net and so forth? You don't view that as a major difference in how you conduct your business, greeting cards?

Mr. DAVISON. I think it was actually Mr. Mayer that had that in his testimony.

Mr. MAYER. Right now this is an unfolding scenario. People are experimenting and we don't know exactly where it will go.

We believe that greeting cards and tangible mail will exist for a long time because they have characteristics that are different than electronic mail—tangibility, the ability to share a greeting card or letter, the ability to save it.

A number of companies, including Hallmark, are experimenting with electronic technology, but it is very new.

Our products convey a lot of emotion, and that's very hard to deliver electronically. So we are not sure exactly where it will fall.

Mr. DAVISON. Senator, Could you imagine sending someone an E-Mail sympathy note, or would you send them a sympathy card?

Senator SMITH. I understand. My question was whether you feel that it is a threat.

Mr. DAVISON. We don't know. We recognize that it will change our business.

Senator SMITH. I want to comment on one of the things that I'm finding as we are now beginning in the Senate to get up on the Internet.

Just for the benefit of all, I find that people are more blunt in what they will send us on the Internet than what they are willing to sign at the bottom of the written page. We start getting a little profanity, a little more blunt talk about how they really feel about us than they might be willing to write us.

I'm reminded of the story that has been told before, I'm sure. But I had an out-of-state constituent who wrote to me, and really used just about every word of profanity that has been known to mankind throughout the ages. It really hit me hard. He signed his name, which was amazing because usually they don't do that. But I wrote back a note to him and said that I thought he might like to know

that some moron has been out there sending this trash and signing his name.

But it is true that I find people tend to be willing to say more and to be more aggressive and more confrontational, more blunt, sometimes with more use of profanity on the Internet than they otherwise would be. I don't know where that is going to lead us, but that's something that I find.

I don't know how that is going to relate to your business. You are not in the business of sending profanity. But I just put that out as a comment if anybody wanted to respond to it.

Mr. MAYER. Well, I think you are right. Communication will increase, and electronic communication will make it a lot easier.

A lot of communication is transactional, and some of it we would call straightforward, and then we are primarily an emotional communication. So we would guess that ours is the least amenable to electronic, although some of it will be.

Senator SMITH. In many ways, though, if you are sitting at your computer and it is your brother's birthday tomorrow and you forgot and you didn't get the card out, if he has an Internet connection, it is almost more personal because you took the time to put it into the Internet and correspond with him via computer rather than send him a late card.

Mr. WEISS. Although we believe that both should happen. Catch him on the birthday and then give him something tangible after the birthday.

Senator SMITH. Well, I have always wanted to steal the Hallmark line for one of my campaigns, that when you sent Smith to the Senate you cared to send the very best, but I won't do that.

Senator STEVENS. Thank you for relieving me. I have to again apologize. I told the Senator he ought to represent a public land State and have to go back time and time again to try and convince the Senate to keep the commitments that were made to a State in years gone by.

Let me see, gentleman, if we have some basic areas of agreement. I think we do from what I hear.

You all believe in universal service for the first-class, monopoly mail?

Mr. DAVISON. Definitely.

Mr. MAYER. Absolutely.

Mr. WEISS. Absolutely.

Chairman STEVENS. And you believe that we should have mailbox protection, you can't use the mailbox unless you are using the mail? Have you crossed that bridge?

Mr. MAY. I personally do. Our associations haven't taken a position. I don't know that we have thought about that issue so I hesitate to answer.

Chairman STEVENS. I think it is going to become more and more of an issue as we think about partial privatization of the Postal Service.

Are there any other services that you think should have a monopoly?

Mr. DAVISON. Other than first-class?

Chairman STEVENS. Yes.

Mr. MAY. Mr. Chairman, third-class letters are also subject to monopoly.

Chairman STEVENS. They are not totally a monopoly yet.

Mr. MAY. You cannot send a third-class letter by any other means except the Postal Service or you commit a civil and criminal violation.

Chairman STEVENS. We have what amounts to third-class mail being sent by UPS and FedEx. I think there may be a situation where it could be protected by the Postal Service, but I don't see it having been asserted. I don't think we can really say it is a monopoly any longer.

Mr. MAY. The Postal Service has created exceptions to monopoly for time-critical material, and in effect, the Postal Service said, "Look, if we can't get it there by regular letter mail in the time you need to have it there, you may use another means."

And they have a test for that, the fundamental test being that if you are willing to pay twice as much as it would cost you to send it by the Postal Service, it is conclusively presumed to be time critical and therefore an exception to the monopoly. This is an exception that the Postal Service itself has granted the monopoly.

Chairman STEVENS. I understand, but they have granted it and it is no longer really protected because they are not enforcing it. I think the only thing that is really enforced right now is the first-class letter.

Mr. MAY. No, they are enforcing regular third-class letter mail. They are indeed enforcing that monopoly. Absolutely.

Chairman STEVENS. I won't argue with you, but only when it is a subjective decision by the sender that there is a time consideration. It can go by other means if they make that decision.

As a matter of fact, I sent a birthday card the other day by one of those other services because I was just so late I knew I couldn't get there otherwise. Now, I don't think that we have a total monopoly there.

You sort of vary on Postal Rate Commission concepts. The tone I hear is that if there is a competitive reason to change a rate for a bulk mailer, perhaps the Postal Rate Commission delays should be circumvented by management in order to preserve the loss of business.

Mr. WEISS. We would disagree with that. We believe that if you don't have the checks and balances of the Postal Rate Commission in place, even in markets where there is competition, the mere fact that those rates are coming down in the third-class or other classes, somewhere those institutional costs have to be picked up, and that will unfairly shift institutional costs to first-class mailers.

Mr. MAY. Mr. Chairman, the only thing that we are talking about that is subject to competition are publication mail—that's in second class—and catalogs in third-class, and all parcels, fourth class. That's the only thing that is subject to competition. The Postal Service has a monopoly on everything else.

The question is how should the rates be set on those things that it does not have a monopoly over and therefore must compete in the marketplace for. And our argument is that unless some flexibility is given to the Postal Service in getting new products to the market and in pricing and doing deals, they are going to lose that

business to the competition, and if that business is lost it is not going to help the greeting card people. It is not going to make a contribution to overhead because it is not going to be there.

Chairman STEVENS. Well, clearly, there are some examples we have heard where there has been a loss.

On the other hand, we look at the concept of uniformity and size. Would you suggest that management can circumvent the Postal Rate Commission if there were a certain dollar value? Must it be related to the bottom line in order to protect other users?

Mr. MAY. No. Frankly, at this point the only full deregulation I would propose is the parcel post and express mail, because that's the only service where there is really full competition and where the consumer does not need the protection of the Postal Rate Commission, because the marketplace will protect those consumers.

But other than that, I'm not proposing that there be deregulation.

Chairman STEVENS. Is volume any consideration?

Mr. MAY. I think that could be a consideration for experimental products, yes. That in circumstances where the amount of the volume was not that significant, that you might have a regulation that allowed the post office a lot more flexibility in doing market testing, yes.

Senator STEVENS. Now, if you want to send a load of Pampers from Anchorage to Unalakleet, maybe you want to send a whole year's supply, a shipment once a week. The volume would be so low that it would not have an impact on the bottom line.

Should they have any ability to negotiate when it doesn't affect the bottom line?

Mr. MAY. Yes. I mean, again, those would go parcel post.

Senator STEVENS. I want to assure you that the other services are not undertaking them because they are losses to start with.

Mr. MAY. I know that, but nevertheless——

Chairman STEVENS. I'm looking at fairness. Somehow or another Mr. Mayer and others are saying there is a fairness matter here. I don't hear a fairness matter in here.

Are we to have universal rates in parcel post?

Mr. MAY. We don't have universal rates, now we have zoned rates for parcel post, but we have universal service for parcel post. Which is why there is service to Alaska.

Chairman STEVENS. You still have the postage stamp rate. You pay the same price to ship within Alaska.

Mr. MAY. Letters, yes.

Chairman STEVENS. Well, parcel post too.

Mr. MAY. But within Alaska, it is a zone when you send from the domestic States.

Senator STEVENS. They are trying to put zones in our State now. They want to put five zones. But some of those zones you would never ship from Anchorage to Unalakleet if that was the case. You would go back to dog sleds. You could get it cheaper.

I just wonder sometimes if what we are looking at in terms of the Postal Rate Commission is a change of function. Do we want a change in function or do you want some exceptions for the function?

Mr. MAY. I really think we are talking about exceptions.

Chairman STEVENS. You are talking about preservation, Mr. Mayer?

Mr. MAYER. Yes. Although it may well be that some of the exceptions, or the flexibility in pricing, might be appropriate with the proper safeguards.

A comment on what Mr. May was talking about. We would love to see the Postal Service more competitive in all of its classes of mail, but not through price adjustment alone.

If their costs were lower, they would be able to charge lower prices and still generate the contribution to institutional costs that they now provide.

Our fear is that if price alone is cut, then they may be more competitive against other services, but the first-class mail user will end up paying all of the institutional costs.

So if we get some of these other improvements that reduce costs, then they would be able to reduce price and still contribute.

Chairman STEVENS. Are you all familiar with the previous hearing we had with the people from foreign nations who have come in and told us about some of the innovations they pursued?

Mr. MAY. Yes, I am, Mr. Chairman.

Chairman STEVENS. Do you believe that we should look to making part of the Postal Service an investor in their own activity?

Mr. MAY. Not really. And I have frankly found most of the testimony really not analogous to the situation in the United States. Those foreign postal administrations, the volume in any one of them is insignificant compared to the volume and complexity of delivering mail to the United States.

Which doesn't mean we can't learn from them. Certainly, if they have a good idea we ought to take it. I didn't think they had a lot of good ideas.

Chairman STEVENS. Mr. Gitlitz suggested that maybe there should be a transition toward change in the postal system, toward a form of privatization. Have any of you thought about that concept?

Mr. MAY. Well, I certainly have, and I know that the Chairman has asked the GAO to do a study of the consequences of that kind of change, or what would happen. And we all are eagerly awaiting those results.

But our members do not want any changes taking place there unless we know what is going to happen, and we don't know what is going to happen. And I think that's what the greeting card people are fearful of, too. But nobody knows what would happen if you start removing the protections of the monopoly.

You can guess, but we really don't know. I didn't understand Mr. Gitlitz really to be saying that. I know Mr. Volner said that clearly he did not believe that any changes needed to be made in the monopoly at this time.

Chairman STEVENS. That's my understanding. But I think he hinted that it might be possible to make transitions on a step-by-step basis.

I'm forced to look at your comments, Mr. May. If any one of you gentlemen had a company that absorbed or really took over from a former company, a former ownership, and you took all the liabilities, and you found a situation where the former company had left

with a prior ownership the responsibility to pay for retirement, are you saying retirement of people who were part of the liability structure you have assumed, that it would be improper for you to be asked to pay the cost of their retirement?

Mr. MAY. Well, I was the general counsel of the Post Office Department when Larry O'Brien proposed reform, and I worked on that. And I also lobbied heavily through the early 1970s on postal reorganization. So I know a little something about what was intended.

A deal was made between the Congress and the Postal Service and its customers, and that deal said that the U.S. Government was going to pick up a fair amount of the costs that were sunk into this system because of postal pay systems and retirement systems and health systems and the future.

And frankly, I don't think that what has been happening in the last 7 or 8 years is consistent with the understanding that was made. And none of this happened when post office was on-budget. Nobody had any interest in doing these reconciliations until the post office went off-budget, at which point they suddenly became a source of cash that would not create red ink.

Chairman STEVENS. No, I disagree. What we are doing—and we just had to do this in this budget process right now—we are paying for the cost of retirement for those people who were retired in days gone by whose retirements have been increased every year since the Postal Service went into effect.

Almost every year we had an increased retirement through COLAs. They were not in effect at the time the old Post Office Department went out of business and the Postal Service took it over.

If the Postal Service does not pay toward the deficit that exists coming out of that period, without any offense, when you were there, sometimes contributions weren't made at all during that period to the Civil Service Retirement Fund.

Now we have to make it whole, and the question is should those people coming in under the new system be asked to pay more because under the law the deficit in the Civil Service Retirement Fund is going to be made up by those people who are now currently in the Federal Employment Retirement System.

And if the Postal Service does not make that payment, then, obviously, the taxpayers are continuing to make the payment and it increases the deficit year by year because the additions to the cost of the Social Security Retirement Fund are not being met by the Postal Service.

Mr. MAY. Well, on the other hand, I mean, I know this is a highly technical subject for the nature of this hearing, and certainly to the extent that individual postal employees would be asked to make up that difference, that's not fair either.

But bear in mind that these are costs that go way back, and what Congress is now asked is to ask current users of the postal system, those who are currently using it, to pay for a cost that was incurred years ago when they arguably were not using it.

And as between whether they, a select group of society, should be forced to pay this cost, or whether all of the taxpayers should be forced to pay it, I'd have to say all the taxpayers should have to pay for that, rather than picking out a group who got no benefit

from that and saying we are going to make you pay for it. And that's what has happened.

Chairman STEVENS. Well, you are right. I'm going to be preemptive and just tell you that the U.S. Postal Service owns all the post offices, they own all of the systems there, they own the rights that were created, they own the system that was created. It is producing money. As a matter of fact, it is in the black and the Federal Government is in the red. Yet the people that have the system that is working and have all of the benefits from the old post office, they are saying no, we don't have to pay anything.

Mr. Jensen, tell me how will you be affected by our reform?

Mr. JENSEN. Well, reform is something that obviously we're interested in because of the automation process. For our company particularly, there are some changes that the Postal Rate Commission saw fit to rule upon that has adjusted the piece pound rates, things of this sort.

We see it bottom line as a very positive thing, that the Postal Service needs to continue to address automation and efficiency and what-not. The bottom line for us is it doesn't cost us any more money, but it doesn't save us anything either.

Chairman STEVENS. Well, I understand that the greeting card people make quite a point out of the fact that they rely upon a total system.

Suppose we were to accept the attitude of some of my friends in the House who say just privatize it entirely, cut it loose now, there has got to be people that should be able to pick that up and run it and over a period of years repay the taxpayers for the investment in the Postal Service. How would you be affected if we did that?

Mr. JENSEN. We think it would affect our business grievously. We mail to people throughout the country, the person who lives in North Dakota that has a town of 300 people as well as New York City. Most of our customers, fully 70 percent of our customers, use the U.S. mail to return an order for a product that they wish to purchase from us.

So we feel that it would affect us dramatically in that regard for the advertising side of the business, as well as the correspondence that we share with these particular customers throughout the United States as well. So we think that would affect us dramatically.

Chairman STEVENS. But you do think, as everyone else has, that the system can be improved and should be improved?

Mr. JENSEN. Yes, sir, I do.

Chairman STEVENS. And you, Mr. Rebello, tell me how your function relates to the postal system.

Mr. REBELLO. Well, we rely totally on the postal system to do business. If the Postal Service were sold and torn apart today, I'm sure that we would find a way to survive.

We would probably be a lot smaller company. There would be jobs impacted not only in Colorado Springs, but probably in the rest of the country that we rely on vendors to produce products, to get our catalogs ready, and to get them to our customers.

But I think the biggest impact is that if the Postal Service were privatized or broken off or sold or however we want to look at this

service or this function that it does would come to the customers in remote areas.

I don't know of any of the people in the catalog business, and I would have to look real close to see if we could cost-justify mailing catalogs into North Dakota, South Dakota, Alaska, and whether we could afford or find somebody who would then ship the product to those remote areas.

So I think our customers would be impacted the most, and I don't think that any of us want that.

I think the one thing that I haven't heard mentioned that I think is a big part of this system is that today the mail is secure. We believe in the security of the mail, and we count on the mail system that when we mail either a correspondence or a parcel or a catalog to a specific customer, that that system is secure enough that we know that it typically gets there. I think that's a big aspect of our business.

Another aspect that has not been touched upon at all of what the Postal Service provides to our customers is the security itself, the security of shop-at-home, etc., which we have to maintain that system.

Chairman STEVENS. An old friend of mine used to say, If the system ain't broke don't try to fix it.

Is this one broken bad enough that we have to really reform it substantially?

Mr. MAY. I don't believe so. I don't believe it is broken that bad. I think you do have to make some adaptations and some modernized rate making and classification procedures. Nothing serious.

Chairman STEVENS. How about you, the gentlemen over here from——

Mr. DAVISON. The Greeting Card Association is not advocating for radical reform. We feel that generally most parts of the system are working well.

Concerning the security aspect and your earlier question in terms of use of mailboxes by others, we would be very concerned with any development that reduces the security of receiving mail addressed to a specific individual. That's important in our business. We think it is important generally.

Chairman STEVENS. Thank you all very much. There is a vote on. I would like to get started on the other panel.

I thank you for your courtesy. We are studying your suggestions. Again, Mr. Gitlitz, I'm particularly pleased with that full suggestion.

If any of the rest of you have been looking that over and have some suggestions, we would appreciate having your comments. It would be helpful to us.

We are going to proceed with some form of postal reform, the Postmaster General really demands it. And I think our one last function is to have the oversight hearing and listen to him, and he has asked us now, very strongly, for some changes in this law.

So I do hope you understand that there is an urgency involved and we hope that you will review these suggestions that have been made and let this Committee have your advice.

Thank you very much, gentlemen.

I'm sorry to do this, but I have got 13 minutes to get out there. If you all would summarize and make your statements and tell us what you think we ought to do, I can still make that.

Otherwise we will have to come back, and there are three votes and it will take some time.

Ms. Rush.

TESTIMONY OF TONDA RUSH, PRESIDENT, NATIONAL NEWSPAPER ASSOCIATION

Ms. RUSH. Senator Stevens, thank you, and yes, I will quickly summarize my remarks in the interest of time.

I'd like to introduce myself. I'm Tonda Rush, National Newspaper Association, president and CEO. Thank you for your consideration in including us today in the hearings.

As you know, we represent the community press. Since we were founded in 1885, the Postal Service and the post office have been probably one of our primary concerns.

We have 3,500 weekly newspapers and about 500 daily newspapers. They are heavy users of the mail. And I think it is safe to say that for most of them they would consider the Postal Service *de facto* their circulation manager.

The existence of the Postal Service, its efficiency and its sound operation, is absolutely critical to our industry.

We have three concerns to lay before you today. I would like to say that next week our board of directors will be reexamining our own thoughts about the Postal Service. We know we are in a radically different world than we were in 1970, and we know that we need to make changes in our own industry.

We would like to work with your Committee, and we would like to come back with you in a couple of weeks, if we may, with some written comments as we have finished our own internal deliberations on our thoughts about what might be included in postal reform.

But I think we can easily lay out three principles that we will continue to adhere to to guide our work here today.

First, we are firm believers in universal service. That concept embraces the idea that mail service is available, regardless of geographic, demographic or psycho-graphic status.

We think mailers should be recognized and rewarded for the work they do when they prepare their mail, but we do not believe that discounts purely for volume or for the size of the mailing customer are warranted or are in keeping with universal service and we oppose them.

We believe that favoritism to large postal customers is inconsistent with the Postal Services Federal ownership, and we would also like to note that in the zero sum game of postal rates, that whenever someone gets a discount someone by necessity gets an increase.

The Postal Service has no profits and has no shareholder stake from which to fund market share growth. It can derive those funds from only other mailers.

Second, we are strong supporters of a viable and vigorous Postal Rate Commission.

In the past 2 years we have been hit very hard by the Postal Service. First, we were faced with a 34 percent increase in in-county postal rates in a year when we were expecting, with other mailers, a 10.1 percent increase.

Last year, in a year when there was purportedly no rate change, we faced a 17 percent proposed increase in our out-of-county postal rates.

We were able to persuade the powers that be not to put those rates in place, but I think you would have a very hard time persuading a community newspaper publisher, after these past 2 years for us, that the Postal Rate Commission ought to be weakened in any way.

In 1994, when we faced the in-county threat, our small association encountered the prospect of a six figure litigation bill, which was nearly three times what we had ever needed in the past. And frankly, it was more than many of our newspapers make in a year's net profits.

In order to fund this litigation, we did a fund raising campaign that looked a little like the Perot for President campaign. The average gift was $60, and it came from a newspaper with under 5,000 circulation.

And we had to, unfortunately, probably spend 20 to 40 percent of that money quibbling with the Postal Service over discovery, over data that I think in any other regulated industry would have been available by due process.

It is very hard for us to see our money going down the drain, and we very nearly had to concede on the postal rate simply because we ran out of money.

We believe the Postal Rate Commission should have subpoena power, and that this process should be strengthened so that the cost and the revenue data are available to the Postal Rate Commission, and to the mailers who are litigating.

Third, last fall when the Postal Service announced its intent for the neighborhood mail program and said that it thought that such a program of unaddressed, saturation, direct brokered mail was warranted because small businesses needed an advertising medium, small newspapers were stunned.

We thought that was what we did. It was a big surprise to community newspapers to find its own circulation manager suddenly in competition, potentially, with them for their advertising revenues. And it certainly sent a shot across the bow in our industry to pay attention to the things the Postal Service may wish to do in the future in competing with the private sector.

Finally, we would count ourselves among the admirers of General Runyon. We appreciate many of things that he has done as he has developed the Postal Service, and I think we have had good access and good dialog with the postal managers.

But occasionally something happens that causes us to have pause. As you know, there has been a great move toward automated sorting. However, there is no machine that can sort a newspaper.

And even as we send some of our own first-class mail into the mail stream, we wonder sometimes about it. A couple of weeks ago we were surprised when our own fliers from one of our conferences

came bouncing back to us because the automated sorting machine liked to read our address code, because it was darker than the ink-jet label that we put on to send to the addressee. The mail all went out there and the automated robot sort of recollected them and brought them back to us simply because the automation didn't work.

Those kinds of problems within the postal system obviously would give us great pause if the machines were sorting our newspapers. It sort of makes us wonder if we were better off with the green-shaded clerks that worked in the boxcar in the old days.

But we are looking forward to working with you, and we hope that as we go forward into this new world of the new Postal Service that we will see a rededication to universal service, that we will see a Postal Service that is dedicated to delivering print material, and to doing it soundly, efficiently and with rates that we can afford to use.

Thank you, Mr. Chairman.

[The prepared statement of Ms. Rush follows:]

PREPARED STATEMENT OF TONDA F. RUSH

Mr. Chairman, we would like to thank you for inviting us to share our views with you today as the Committee embarks upon an examination of the future of the Postal Service. This is the perfect week to begin such a careful prospective.

I awoke on March 12 just 2 days ago to discover that it was the anniversary of the founding of the Post Office, the predecessor agency to our U.S. Postal Service. The anniversary date is shared with the birth of Edward Albee, the death of Anne Frank and the ordination of the first female Anglican priests. If there ever were a day that embodied the full scope of tradition, change, creativity and tragedy, March 12 would have to be it. Given the gravity of the task ahead, then, Mr. Chairman, it would seem appropriate to begin in this, the anniversary week of universal postal service.

Mr. Chairman, you have asked for interested parties to explain their vision of the future of the Postal Service. My guess is that you are going to receive as many different visions as you have witnesses at these hearings.

One thing that we will all share, I predict, is a firm belief in the need for a federally mandated Postal Service; one that guarantees that universal service will continue far into our future. But, predicting the future of communications as far ahead as 5 years is a challenging, almost impossible task. Our technology in this area is changing at a breathtaking pace. Many of us, including the National Newspaper Association, are attempting to analyze what may be taking place in the future of mail and every other communications mechanism.

NNA, as you know, represents the community press. Our 4,000 members include most of the weekly newspapers and a third of the daily newspapers in the country. We were founded in 1885 and one of our primary missions throughout our history has been to work with the postal system for fair rates and, most important of all in our time-sensitive business, efficient delivery.

Our industry was among the pioneers of presorting as we worked with local postmasters to make our mail as easy to manage as possible. Since 1970, we have worked directly with this Committee and its predecessors to bring about a smooth transition from subsidized rates and we benefited greatly, Mr. Chairman, from your leadership as we found the key in 1993 to ending revenue forgone.

Today, virtually all of our members are heavy mail users and, indeed, many of our weekly publishers consider the local postmaster their circulation manager.

The NNA Postal Committee and our Board of Directors will be gathering here in Washington at the end of the month to address many of the issues you are interested in. When our meetings are concluded we will have developed a list of principles that we believe should guide postal reform and we would hope to present these in writing to your Committee.

Today, I would like to outline for you three basic needs for the future that will guide our discussions.

1. *Universal Service.* The concept of universal service must continue to be the fundamental goal of the Postal Service. Irrespective of technological evolution or soci-

etal change, the need for a delivery service that treats the nation as one will continue.

Universality includes the concept of geographical as well as demographic fairness. Hand in hand with the concept of the monopoly enjoyed by the Postal Service goes the notion that no one will be singled out for better treatment or inferior treatment based upon where they live, their economic circumstances or the desirability of their purchasing power to a business.

The Postal Service wants to compromise that vision with a favoritism concept involving volume discounts and contract rates. There are basic fairness issues involved in these concepts when promulgated by a Federal Government service. Moreover, there are economic problems as well. The biggest problem is that the Postal Service has no profits to absorb lower rates for favored customers so it must ask its regular customers to pay extra in order to reduce the rates for the larger mailer.

This approach may be intended as cream-skimming or market share building or simply a mimicking of for-profit business, but it is undeniably discriminatory and should be prohibited by Congress.

The Postal Service is making the incredible claim that it can reduce rates for one or a small group of customers and reduce rates for all the rest of its customers as well. This Committee ought to be very skeptical of such a claim—unless it is based upon a more serious cost-cutting or down-sizing than we have yet seen. We urge the Committee's skepticism of such a claim.

2. *Postal Rate Commission.* We need a stronger, more effective Postal Rate Commission with the authority to set postal rates and to subpoena Postal Service cost and revenue information. The Commission has the weakest set of regulatory tools of any regulatory agency in Washington even though it oversees a $55 billion monopoly whose operations closely affect virtually every portion of the American economy.

And the Postal Service is the only regulated monopoly in the country with the power to virtually set its own rates as well as to determine by its own regulations the nature and scope of its own monopoly and the degree to which it will permit its competitors to compete.

The importance of the Postal Rate Commission can best be demonstrated by the request of the Postal Service for a 34 percent increase in the postage rates of in-county newspapers. In 1994, as the rest of the mailing community prepared for a negotiated 10 percent rate increase, in-county newspapers were stunned by this proposed 34 percent hike. If it had gone into effect, it would have cost some of our smaller members the equivalent of their profit margins for that entire year. After protracted litigation at the Postal Rate Commission and after overcoming the Postal Service's unwillingness to release cost and volume information, NNA finally received notice from the Postal Service itself that its data were bad and that, instead of a 34 percent increase, the in-county rate should have been decreased by almost 2 percent.

I want to acknowledge the serious and laudable efforts of the Postal Service economists in finding the errors. The root of the problem turned out to be in the troubled In-Office Cost Systems (IOCS) which have been the source of much litigation before the Commission. We do not know if the errors in the system will have been fully corrected before the next rate case, but we do know that without the recourse to the Postal Rate Commission, small mailers like ours would have no means of defending against a monopoly that simply did not have the incentive to correct the errors before they were passed on to the mailers.

Without the Postal Rate Commission, newspapers would be paying 34 percent extra today and future increases would clearly be based upon a highly inflated rate structure.

Incredibly, the Postal Service followed up that proposal with an attempt to raise our out-of-county rates by 17 percent and to introduce the equivalent of volume pricing into second-class mail regulations. That, too, was defeated at the Postal Rate Commission. It would be a difficult task today to convince a newspaper publisher that the Postal Rate Commission ought to be weakened in any way after it has saved us twice in 2 years.

In both of these cases, Mr. Chairman, NNA was faced with its own daunting challenge and that was to figure out how to pay for the cost of defense. In an association where a $10,000 retained earnings net makes for a very good year, the prospect of coming up with $100,000 or more for litigation was not pleasant. We did it, Mr. Chairman.

I'm afraid our fundraising campaign looked a little like the Perot for President hotline. Most of our donors were weekly newspapers with under 5,000 circulation and the average gift was $60. Painstakingly, we built our litigation fund and, fortunately, it turned out to be well spent.

What was galling was having to spend $40,000 or $50,000 of these hard-won dollars fighting with the Postal Service over discovery of basic cost and revenue data that we needed to check their—as it turned out erroneous—figures against our members' own postal records. All we wanted in one case was a list of post offices where statistics were developed so we could double check against newspapers' records. But the USPS ran the clock interminably and we had to spend money against its staff lawyers' time to get data that in any other regulated rate proceeding would be available as a part of due process.

Every lawyer here can tell some similar tales, I would guess. But it is a poignant one for us. We very nearly had to give up the battle and accept the rate increase because we were about to run out of money.

We therefore find good cause to urge you and the Committee to examine subpoena power for the Commission, particularly if the Postal Service continues to insist it must build volume by branching out into more speculative enterprises. If it is permitted to compete on its own terms and the watch dogs are chained, Mr. Chairman, how will the public be protected?

3. *Competition with the Private Sector.* It has to be a question for this Committee to decide if it wants its vision for the future to include a Federal agency competing with private sector firms that are presently serving the public.

The Postal Service, of course, wants to be able to "compete" with the private sector using its advantages of monopoly, freedom from taxes and governmental status. On the other hand, the private sector competitors (which include newspapers) must pay Federal, State and local taxes, property taxes to their communities and meet a myriad of Federal, State and local operational and zoning regulations the Postal Service is exempt from.

This Committee heard testimony recently from foreign postal administrations. Sweden's situation is quite instructive with regard to competition. When postal competition was authorized a private firm began operations in the Stockholm area. Sweden Post simply lowered its rates 7 percent in Stockholm and, happily, no more competition.

The advent of a proposed "Neighborhood Mail" service last fall, right after we had opposed the Postal Service 2 years in a row with respect to our own rates seemed like a chilling threat after hearing the Sweden Post story. Could the Postal Service really have been serious that it wanted to start an unaddressed saturation mail advertising brokerage because local small businesses had no advertising outlet—even when it is carrying possibly 50 to 75 million or more community newspapers in its mailstream every week? If ever there had been a wakeup call to our industry, Mr. Chairman, that was it.

Mr. Chairman, we do not have a crystal ball to foretell the Postal Service future. We sometimes think we believe in it more than its own managers do, since we seem to have a more universal understanding of universal service. But we do value its service tremendously.

We admire many of the actions General Runyon has taken to improve them. One we're not too sure about is the drive to eliminate mailer sorting in favor of multi-billion dollar machines. Just last month a packet of our fliers, properly addressed, came bouncing cheerfully back to us because the multi-line optical character readers liked to read our darker return address better than they liked the inkjet printing on the address label. If this is what the machines are going to do for us, we might like to go back to the clerk in the green eyeshade on the rail cars, thank you.

We do have many concerns and we share your belief, Mr. Chairman, that it is time for Congress to begin thinking how its postal corporation should work in the 21st Century.

We want to work with this Committee and the Congress to help implement these three fundamentals to help build a better, more effective Postal Service for the future. The Nation's community newspapers are dependent on the Postal Service for much of our distribution. We do not wish to see it weakened in any way.

Chairman STEVENS. Thank you, and thank you for your courtesy.

Gentlemen, I'd like you to split about 5 minutes, unless you want to come back. I'll be glad to come back and listen to your testimony.

Why don't you proceed, Mr. Sturm.

TESTIMONY OF JOHN STURM, PRESIDENT AND CEO, NEWSPAPER ASSOCIATION OF AMERICA; ACCOMPANIED BY WILLIAM WILSON, TARGET MARKETING DIRECTOR, KNIGHT-RIDDER, INC.

Mr. STURM. My name is John Sturm. I'm the president and chief executive officer of the Newspaper Association of America. We have 1,500 members. We represent about 85 percent of the daily circulation of newspapers in the United States.

To my left is Bill Wilson, director of Target Marketing, for the Knight-Ridder, Inc., in Miami. He is here for the volleys, I'm here for the lobs.

Let me quickly say that I agree 100 percent with the testimony of my friend and colleague, Tonda Rush.

Universal service is one of the most important things that we can retain for our Postal Service system today. And I think she has quite well highlighted some of the key factors that we have to consider as we move forward.

I didn't think in my first time testifying that I'd be between a United States Senator and a vote, but I will try to be very careful and very quick with my comments today.

Senator STEVENS. These votes weren't supposed to come until 12:30, but we have missed the timing of this.

Mr. STURM. Mr. Chairman, I think if you listened, as you did today, to a lot of the testimony that was given, you have a couple of public policy choices facing you at the present time.

First and foremost, we could reaffirm the system that Congress put in place in the early 1970s. We can stay with universal service, non-discriminatory rates, and I believe what the American public really wants out of their postal system, a system that will simply get their mail from point A to point B efficiently and on time. And I would urge you to move in that direction.

Another public policy choice is to go in a completely different direction and totally privatize the Postal Service. That is certainly a legitimate choice. I'm not necessarily advocating it at this point, but it is a choice where the Postal Service gives up the monopoly and has no more special privileges.

What I am concerned about is that what we are heading for, and frankly, I think this is also what the Postmaster General would like—a hybrid system where the Postal Services retains its monopoly privileges—no taxes, *de facto* antitrust monopoly, no shareholders, no dividends, the whole bit, and then it acquires a number of little gimmicks that it has suggested that this Congress give them immediately, the most serious of which is the ability to set prices pretty much on its own, either through pricing flexibility or volume discounts.

Let me suggest to you that this is about cost, not price. Everyone in this room has agreed on one central principle, that we must have a more efficient, productive Postal Service, since 80 percent of their costs are involved with labor. There is no dissent in this room to the notion that what we should be doing first and foremost is giving the Postal Service the power to deal with their own internal management and cost problems.

That takes us a long way. In a system in which the service cannot drop, has shown no ability to drop its costs, we cannot add to

the Postal service's powers the ability to give volume discounts—because those costs will invariably be shifted to someone else.

So let me suggest to you, if I can offer just two thoughts to take home. One, we may be going at this in the wrong sequence. If we give the Postal Service—and Postmaster General Runyon, when he appears in front of you, will have quite a few things that he will suggest to you—things that he can do if you will give him the power to become more efficient, labor management, etc. I think that's where you have to start before you even consider going the pricing flexibility way.

Because ultimately what you have seen on these panels in that the big mailers prefer pricing flexibility and the little mailers don't like for the most part because we feel, even though I have some large companies, from a competitive standpoint we will lose if we have volume discounting, because we will invariably get more costs laid on us, as will first-class mailers.

Chairman STEVENS. Mr. Wilson, I have about 3 minutes. I hate to do this, Mr. Sturm. We have about 3 minutes to leave and I have got to go.

Mr. STURM. The good news is he has no prepared statement.

Chairman STEVENS. I thought you had some zingers for me.

Mr. WILSON. I have no prepared statement, just answers, sir.

Chairman STEVENS. Go ahead then.

Mr. STURM. Thank you, sir. Let me suggest one other thing. What we have to have going forward is a better postal system. We all rely on the postal system.

What we don't want is a postal system that has all of the monopoly privileges and is trying to act like a business at the same time, because it will not work. It is not good for consumers, it is not good for customers, and it certainly is not good for those of us who have to compete with essentially a monopoly service in downstream markets.

If you don't think the Postal Service doesn't want to compete with private industry, I would suggest perhaps that you read Postmaster General Runyon's comments when Publisher's Express went out of business. "We ran them out of business." I can't say I'm sorry to see them go.

This is a government agency running a private delivery service out of business and acting pretty happy about it.

The second thing this government agency does under the current setup, which would get worse, is it picks winners and losers. This is an ad that was in the *Washington Post* and the *Wall Street Journal* recently. While we appreciate the ad revenue from the Postal Service, the fact of the matter is this is the Postal Service saying direct mail is more influential than TV advertising, so why do they call it junk mail?

Here is the Postal Service advertising in favor of a private business. The winners are in their opinion, the direct mailers. The losers are newspaper advertising and television advertising.

Thank you.

[The prepared statement of Mr. Sturm follows:]

PREPARED STATEMENT OF JOHN F. STURM

Good morning Mr. Chairman, distinguished Members of the Committee.

My name is John Sturm, and I am the President and CEO of the Newspaper Association of America (NAA). With me today is Bill Wilson, Target Marketing Director for Knight-Ridder, Inc., a multi-media company that owns and operates 31 daily and 10 non-daily newspapers throughout the United States.

NAA is a national trade association serving more than 1,500 member newspapers in the United States and Canada. NAA members account for more than 85 percent of the U.S. daily circulation and more than 60 percent of our members have a daily circulation under 25,000.

Thank you for giving NAA the opportunity to appear before you today to share our thoughts on the future of the postal system. We look forward to working with you and your staff on the difficult issues the Committee will face today and in the future.

You have asked that I address the newspaper industry's vision of the Postal Service in the next 5 to 10 years, as well as make several specific recommendations on how the Postal Service could be modernized. To understand our views on this issue, let me begin by describing the complex relationship between America's newspapers and the Postal Service.

Newspapers and the Postal Service

Newspapers make extensive use of the postal system not only in Alaska, but throughout the United States. We spend hundreds of millions of dollars annually in First-, second-, and third-class postage. Yet, while a given newspaper is often one of the Postal Service's largest customers in any local area, collectively, newspapers are not considered significant customers by the Postal Service. Additionally, many of our members justifiably feel that the Postal Service has targeted the newspaper industry over the years, seeking to drive advertising revenues out of the pages of America's newspapers and into direct mail. Unfortunately, both of these experiences—as well as ventures such as "Neighborhood Mail"—have led to a profound distrust of the Postal Service in many quarters of our industry.

Thus, the newspaper industry has a very complicated relationship with the Postal Service, and many USPS pricing decisions affect newspapers interests both as customers and as competitors with certain segments of local, direct mail.[1] Indeed, our industry depends upon second- and third-class delivery for our advertising and editorial products and upon First-Class for delivery of our advertising and circulation invoices.

Given this multi-faceted relationship, newspapers have no desire to weaken the Postal Service as an institution and need a strong postal network.

Our Vision Of The Postal Service

A. The Postal Service Should Remain A Public Service Devoted To Universal And Nondiscriminatory Service.

Almost a year ago, when NAA testified before Chairman McHugh's subcommittee in the House, we expressed our concern that the Postal Service was at a crossroads and in dire need of Congressional direction. We sensed that there was a crisis of direction and purpose at the institution, and that the institution seemed more interested in serving a handful of large mailers and in competing with the private sector, than in serving the American public.

Nothing that has transpired since our testimony last year has lessened our concern. Indeed, several developments, such as the Neighborhood Mail fiasco, have intensified our concern, as has the Postal Service rhetoric on contract rates and volume discounts.

Today, more than 25 years after the Postal Reorganization Act, the Postal Service stands at a turning point. One direction would continue the public service function of the Postal Service. This direction emphasizes that the Postal Service is precisely that—a *service* provided by the nation to its citizens on a nondiscriminatory basis—and stresses service to rural areas and certain public functions of the system. A sec-

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[1] Newspapers compete with local, non-targeted direct mail companies, many of whom mail advertising circulars on a saturation basis. In this sense, newspapers compete in a "downstream" market (advertising) from the Postal Service (distribution). However, as a competitor in a downstream market, newspapers feel the effects of the Postal Service's enormous statutory advantages and the power these advantages give the Postal Service to distort competitive markets. These include its monopoly on most postal volume and the letterbox; its practically unlimited ability to borrow despite its poor equity position; its exemption from antitrust liability; and its freedom from State, local and Federal taxes. Newspapers are especially wary of the Postal Service's ability to alter the competitive balance inefficiently by shifting overhead costs from "competitive" to monopoly services.

ond direction that some seem to prefer would create powerful economic incentives for the institution to abandon if it can—and seriously downplay if it cannot—service to rural areas and the public functions that distinguish our present system.

The first view of the Postal Service's future recognizes that the provision of postal service is a fundamental government service that is to be offered to the citizens of this country on a nondiscriminatory basis. It is a view that holds that the Postal Service should not be allowed to enter private markets and pick and choose among competitors, consciously seeking to favor some in the market and disadvantage others. No special deals for one business over another. No special deals for competitive reasons. This view fully realizes the tremendous anti-competitive capacity that exists when a monopoly is left unchecked to wreak havoc in competitive markets. It is a view that encompasses the need for social values, such as the nonprofit rates, and it is a view of the Postal Service in 5 and 10 years that NAA strongly endorsees.

The other view holds that the provision of postal service is a business, and should be provided—like a business—on an unequal and discriminatory basis, with the provider of the services picking and choosing on what terms it wishes to deal. This view would hold that the creation of "alliances" with one private sector party, parties or industry, to the detriment of another private sector party, parties or industry is not only perfectly acceptable, but also is a desirable way for the government to operate. The economic incentives created by this view would lead an enterprise to pick more economically attractive markets over less attractive markets—suburban and urban markets over rural. In short, it is a view that is fundamentally and inexorably inconsistent with a philosophy of providing universal service on a nondiscriminatory basis to all Americans in all corners of our country at uniform rates.[2]

It is a distressing commentary that the Postal Service has already pushed its way past the starting point of this second—and we believe fundamentally mistaken—direction, and has done so behind closed doors and without a public debate. It has chosen a path at odds with its public service and nondiscriminatory mandate. It is a direction that focuses on leveraging its monopoly to compete with the private sector, as evidenced by Postmaster General Runyon's recent speech where he proudly marked the Postal Service's success at running a private sector company out of business.

It is astonishing to hear that a government bureaucrat today can publicly celebrate having driven a private company out of business. It is equally outrageous that the Postmaster General seems to want to run even more private companies out of business as well. Over the last several years, the Postal Service increasingly has chosen to use its statutory monopoly on letter mail and the letterbox to leverage its ability to compete where it lacks a monopoly (such as parcel delivery and urgent delivery) or where mail volume is in part dependent on one competitor in a market (such as saturation mail).[3] The Postal Service achieves this leverage by using what is known as "demand pricing" to shift an ever-increasing share of the overhead and common costs of the postal system to services and customers that legally lack practical alternatives.

The recent postal reclassification proceeding contains examples of the Postal Service's continued focus on institutional cost shifting. In the reclassification case, the Postal Service convinced the Postal Rate Commission to recommend the creation of an "Enhanced Carrier Route" subclass in third-class, thereby setting the stage for future large shifts in the institutional cost burden away from this allegedly "competitive" subclass and onto monopoly classes.

Such cross-subsidies[4] are far from an academic concern; the financial well-being of consumers, the appropriate use of scarce investment resources, and the fate of

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[2] Contract rates and volume discounts are two pricing mechanisms designed to give mega-mailers special deals *at the expense* of smaller mailers and rural mailers since neither of these pricing mechanisms lead to either higher income or lower costs. Contract rates or volume discounts for mega-mailers are not new ideas. Both have been around for over a decade, and have been regularly rejected by the vast majority of the postal community.

[3] Unlike most other regulated monopolies, the Postal Service has no incentive to maximize profits since it is a government agency and not a private company. Economists have suggested that the Postal Service attempts to maximize volume which gives it strong incentives to cross-subsidize. This is because, if a monopolistic institution's goal is to maximize volume, an effective (but fundamentally inequitable and economically inefficient) way to do so is to shift costs off of volumes that have competitive alternatives (Express Mail, Parcel Post, saturation mail) and onto mail held captive by the Private Express Statutes, which in the case of the Postal Service is largely First-Class mail.

[4] We are not using the term "cross-subsidy" in the sense of merely covering what is known in postal ratemaking as "attributable costs." Rather, we are using the term in the same way

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already competitive markets are at stake. Cross-subsidies increase prices for First-Class mailers, who, today, pay more for postal delivery than they should. In addition, increasing rates for these captive consumers could encourage investment and entry by alternate competitors (such as E-Mail, fax, etc.) which otherwise would not occur, thereby causing an inefficient allocation of resources, and hasten the day that electronic alternatives cut into First-Class volumes.

Cross-subsidization also enables the Postal Service to capture market share in competitive markets (e.g., parcel delivery and expedited delivery) at the expense of more efficient competitors.[5] These competitors are prevented from realizing the benefits of their efficient cost structure by the Postal Service's ability to recover part (if not all) of the cost of competing in the competitive market from monopoly ratepayers.

Finally, companies competing with mailers who are offered low mail rates which do not accurately reflect the true underlying cost of providing the service are harmed because these mailers are able to offer lower prices for their services. This is especially true where delivery costs are a significant portion of a competitor's cost structure. For example, if newspapers were the more efficient providers of advertising services, in the absence of "competitively" non-cost-based discounted rates for saturation mailers, newspapers would be harmed by losing business which their cost structure would otherwise allow them to capture. This would occur simply because the Postal Service would have the incentive and opportunity to implement discounts not based on costs through the dumping of costs onto the monopoly. In effect, such discounted prices for some mailers would create a perverse incentive for advertisers to use mail service instead of other, lower cost alternatives. Thus, a competitive market is distorted by the pricing policy of the Postal Service, and society is worse off because scarce resources are uneconomically diverted away from the least-cost producer.

The Postal Service, acting on its own and without any approval from the Congress or the American public, clearly has chosen the second direction. while the second direction would help a handful of the largest mailers who stand to benefit from the cross-subsidies flowing from monopoly mailers, it is harmful to the nation. We simply do not believe that the American public wants a Postal Service that gloats at the demise of private businesses and seeks to establish incentives that inevitably will undermine the basic concept of nondiscriminatory, universal service.

B. Foreign Postal Systems Are Not Appropriate Models.

In this regard, we are aware that some have suggested that our postal system has fallen behind those of other countries, and that we must "modernize" our system and model ourselves on certain foreign postal systems. The notion that foreign postal systems can provide useful models for the United States strikes us as quite unrealistic, for several reasons.

First, while the United States Postal Service is viewed by many as inefficient, it is far *more* efficient than foreign postal systems. Once again, the U.S. Postal Service is far more efficient, not less efficient, than foreign systems.

As the GAO noted in its January 1996 testimony before the joint hearing of the Senate and House postal subcommittees, as compared to any single system GAO looked at, the U.S. Postal Service delivers *seven times* the volume of any of those systems with only *twice* the number of employees.[6] Thus, the notion that the efficiency of the U.S. Postal Service pales in comparison to trendy foreign administrations—a proposition we have heard repeatedly—simply is not true.

Moreover, many of the reforms instituted overseas reflect an implicit policy decision to "reform" postal delivery by allowing a government-owned entity to provide services which can be and are provided by private, competitive firms. The approach of foreign countries to postal reform reflects certain underlying policy judgments that fundamentally contradict U.S. public policy, under which the private sector is

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that most major mailing groups used it during the revenue forgone debate several years ago, and that is to indicate an artificial allotment of overhead costs to a service that would not necessarily otherwise occur, if the Postal Service were a private sector company operating in a competitive environment.

[5] The fact that the Postal Service's attempts to subsidize its parcel and urgent delivery services have not succeeded in capturing market share does not indicate that prices for these services are subsidy free. Rather, the inability to attract market share is likely due to customer perceptions that the quality of service is poor, as well as to the perception that it is worth paying a premium to avoid dealing with the bureaucratic Postal Service.

[6] *Testimony of Michael E. Motley at 2.* If one takes the eight systems that the GAO examined, in the aggregate, one finds that our postal system delivers *twice* the volume with *fewer* employees. *Id.*

considered more efficient than the public sector, and the government is to encourage private sector growth over public sector growth.

Second, *each* of the nations often cited as possible models for the United States, with the exception of Canada—whose system is in fundamental trouble—concentrate primarily on what we call First-Class mail, and very little on third-class mail. In those nations, the primary focus of the post office is generally on the delivery of personal and business letters, not advertising mail. While First-Class mail should be the primary focus of the U.S. Postal Service as well, other mail services seem to receive far greater management attention in our system. Should the Congress feel that the favors the Postal Service has heaped on third-class mail have been inappropriate, and that the Postal Service should return to its fundamental mission, then there might be lessons to be learned from examining First-Class mail delivered by foreign postal systems.

Third, turning to Canada—the one foreign post office which seems to devote more attention to advertising mail than First-Class mail—one finds a system allegedly so ripe with inappropriate cross-subsidies that it is falling apart. In Canada, the government is formally reviewing Canada Post from top to bottom in a "Mandate Review" and will be considering whether to institute a more rigorous pricing system in order to eliminate cross-subsidies and prevent their reoccurrence. The Canadian review will also include an assessment of the long-term mission of Canada Post and a consideration of its competitive (or more accurately anti-competitive) conduct to date. As part of that process, it will consider whether to reorient Canada Post away from competition with the private sector, and refocus it on delivering the general correspondence of the Canadian public. It is interesting to note that Canada is looking to our system and to our Postal Rate Commission as possible models to adopt.

It is important to realize that a Canadian Mandate Review is *not* a normal, routine, or ordinary process. Rather, it is one reserved for situations where the government has a very serious reason to believe that basic problems exist with the current structure and must be addressed. It would be ironic indeed if this Congress were to use Canada Post as a model at a time when the Canadian Government is questioning the actions of its postal institution, and making a thorough reexamination of its mission and operations, and looking to the U.S. system for a possible solution.

As a last point, even if none of the above were true, comparisons between the United States and foreign postal administrations must acknowledge the absolutely enormous differences in geography, population size, and population density between the United States and these countries. Suggestions that New Zealand and Great Britain are useful models ignore the fact that those nations are far more compact than ours, and serve far fewer people. Suggestions that Canada offers a suitable model ignores the tremendous differences in population density between Canada and many areas of the United States, and the resulting size of the cross-subsidies that consequently flow from urban America to rural America in the postal area, and do not in Canada. There is no *prima facie* reason to think that regulatory regimes suitable for postal systems that serve relatively small volumes of mail in relatively small geographic areas offer much useful guidance for a Postal Service that serves 250 million persons across an entire continent—including the vast expanse of Alaska, not to mention the Hawaiian Islands—and yet includes such megalopolises as New York City, Southern California, and Chicago.

Steps to "Modernize" the Postal System

The Postal Service is a very complex institution that affects millions of individual citizens and businesses, and any change in the system cannot be taken lightly. The Postal Service is vital to the economy of this country and to the well-being of thousands of companies, including newspapers. Before undertaking any major change, this Committee must be convinced that the system is indeed "broken," and it must understand the full impact of any quick "fix." The Committee is considering postal reform proposals that haven't been considered by the Congress in 25 years. Hasty decisions in this area will do more harm than good.

The newspaper industry believes that the Postal Service must return to basic "First Principles," and concentrate on its statutory mission of obtaining the best possible service for the public at a reasonable rate. The Postal Reorganization Act establishes—correctly we believe—that the basic function of the Postal Service is "to provide postal services to bind the nation together through the personal, educational, literary, and business correspondence of the people."[7] Moreover, Section 101 of the Postal Reorganization Act provides that "[t]he United States Postal Service shall be operated as a basic and fundamental service provided to the people by

[7] 39 U.S.C. § 101(a).

the Government of the United States, authorized by the Constitution, created by Act of Congress, and supported by the people."[8]

This Committee should reaffirm those principles.

Moreover, consistent with this position, we offer additional thoughts for Congress to consider as a part of that reaffirmation:

- A modern Postal Service should provide universal service at nationwide, nondiscriminatory rates with high quality service. As part of that reaffirmation, postal performance data should be publicly available to all.
- A modern Postal Service should be financially sound. The Service should eliminate its negative net equity position and obtain better control over its costs. The Postal Rate Commission should have the tools it needs in order to ensure that rates appropriately track costs.
- A modern Postal Service should not set rates and establish services to intentionally compete with private sector firms or intentionally interfere with private sector markets.

Finally, this Committee should make its decision—just as the Kappel Commission did years ago—on the basis of what is best for the country, even if that is *not* what the Postal Service thinks is best for it. This Committee must carefully seek out and discover the underlying facts of this matter, and not simply rely on the unsupported rhetoric of the Postal Service and a small handful of its large allies.

A. Universal Service

Congress should reaffirm that the Postal Service is a fundamental service provided by the national government to the citizens of this nation, in order "to bind the Nation together." In particular, we believe that Congress should reemphasize that universal delivery service at *nondiscriminatory* rates is the core mission and fundamental purpose of the Postal Service. Actions by the Postal Service inconsistent with this fundamental mission should no longer be tolerated.

The importance of maintaining universal service and maintaining and improving service quality cannot be overstated. These postal obligations are properly mandated by the Act, demanded by the mailing public, and should be maintained.

Regrettably, the quality of service provided by the Postal Service has declined since Reorganization. For example, in 1978, the Postal Service abolished mail delivery to residence doorsteps for new homes, instead requiring customers to pick up their mail at cluster boxes up to one-half mile away from their homes. More recently, a significant deterioration in the consistency of mail service was observed in the late 1980s; the Postal Service responded by relaxing its service standards.[9]

Even after the revised standards were put in place, however, the overall speed of delivery decreased.[10] Delivery reached its most recent trough (of which the public is aware) when the results of a Price Waterhouse study reported that Washington, D.C. had the worst mail service in the country during the quarter ending May 27, 1994; only 60.6 percent of First-Class mail arrived on time.[11]

While quality has increased somewhat since then, the Postal Service still measures its reliability in terms of misdeliveries per 100. Daily newspapers measure their misdelivery rate for morning newspapers in terms of less than 1 misdelivery per 1,000. That is a scale of reliability that the Postal Service cannot even consider matching, and it is a scale of reliability that many businesses need and that the Postal Service should provide.

Finally, a growing problem in this area is that the data upon which one can base such evaluations seems to be disappearing from the public view. We need accurate, external, and publicly-disclosed measures of delivery service for all classes. The American public deserves to know how good its postal service really is, and how it fluctuates.

In recent years, the Postal Service has contracted with Opinion Research Corporation and The Gallup Organization to measure customer satisfaction for residential and business customers, respectively. In addition, through a contract with Price Waterhouse, the Postal Service obtains a measure of First-Class delivery performance through the External First-Class Measurement System. More recently, the

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[8] 39 U.S.C. § 101(a)

[9] *See,* CRS Report for Congress, *Mail Service in the United States: Exploring Options for Improvement,* at 19 (November 13, 1995).

[10] *Id., citing* U.S. General Accounting Office, *Revised Delivery Standards: Postal Delivery Scores Improved but Service is Slower,* GAO/GGD–93–12, (November 1992).

[11] *See,* Bill Miller, "Post Offices Playing Catch-Up; Workers on Overtime to Speed Up Delivery," *The Washington Post,* July 24, 1994, at B1.

Postal Service has monitored delivery service for second- and third-class mail as well.

However, neither the American people nor this Congress sees much of this information, as the General Accounting Office recently reported. *See GAO, New Focus On Improving Service Quality and Customer Satisfaction, GAO/GGD–96–30 (December 1995).* As the GAO states: "Although the Postal Service has generated valuable information from its residential customer surveys since 1991, it has provided relatively little of the information to Congress" and, in recent years, "has reduced the amount of residential customer satisfaction data and other performance data provided in required annual reports to Congress." *Id.* at 23.

Indeed, the GAO noted that the Postal Service publicly discloses the responses to only consumer question relating to the Service's overall performance for the nation. Moreover GAO noted that from Fiscal Year 1991 to 1994, the Postal Service "reduced the amount of information on customer satisfaction and delivery performance provided to Congress." Not only does the general public receive only a smidgen of information regarding First-Class delivery, but it receives no information at all regarding the Postal Service's delivery performance of second- and third-class mail.

The Postal Service cannot and should not hide its performance from the American people who, after all, are its owners. We firmly believe that the Postal Service must publish regularly all of its performance data and customer satisfaction information. Such a requirement would focus attention on the delivery of First-Class mail and would tend to ensure that other services are not provided or improved at the expense of First-Class.

B. Restoration of the Postal Service's Financial Soundness

The Postal Service's financial condition has deteriorated significantly since Reorganization. In the 25 years since 1970, it lost nearly $9.4 billion.

Three reforms are necessary to redress this problem. First, the Postal Service should restore its net equity position promptly. Second, the Postal Service should gain better control of its costs in the future. Third, the Postal Rate Commission should be given sufficient powers to preserve the fiscal soundness of the Service.

1. The Net Equity Deficit

As this Committee is well aware, the U.S. Postal Service has operated at a substantial net equity deficit since Reorganization. This net deficit stands, as of the last rate case, at about negative $9 billion. The net equity deficit amounts, in effect, to an interest-free loan to current (and past) mailers from future mailers, and is recovered in rates as institutional costs. Since First-Class mailers now pay more than 70 percent of the institutional costs of the Postal Service, this really means that *future* First-Class mailers are subsidizing *current* mailers of *all* classes.

This Congress has made major strides in recognizing the need of the Federal Government to balance its budget and pay off its accumulated debts. The same holds true for the Postal Service, which is an establishment of the Federal Government.

Restoration of its net equity position should be a top priority of the Postal Service. The net equity position is plainly harmful to the Service, for it diminishes its value to the people of the United States, impedes its ability to invest, and forces it to incur greater debt than it would if it had a positive equity position. Moreover, it is our view that full restoration of the Postal Service's net equity position is a basic prerequisite before reforms can even be discussed.

Finally, the Committee should be wary of self-interested mailers that urge that current operating "profits" be used to maintain low rates for themselves as long as possible. Clearly, the paramount concern of such mailers is in preserving low rates for themselves, not in the overall financial health of the Postal Service. The United States Government should not run on a deficit, and nor should the U.S. Postal Service.

2. The Need To Control Costs

Despite the relative efficiency of the American postal system over foreign postal systems, there is a general consensus among mailers that in order to better face the future, the Postal Service must focus more aggressively on controlling its costs. Much of this concern stems from the failure of the Postal Service to capture the promised efficiencies of automation and prebarcoding. The Committee should investigate the situation and try to uncover exactly why these efficiencies haven't been obtained.

Pricing is not the problem, and insisting that it is all about pricing—with all the wild and unruly political discord that this issue engenders—is not going to solve any problems. The problem is cost, not price.

The Postal Service has cried loud and long about its inability to regain the market in parcels and overnight mail that it lost years ago. Service and customer relations

have long been the problem in these areas, and price only a problem to the extent that the Postal Service simply cannot do the job as efficiently as the private sector. If the Postal Service can't match a parcel or overnight competitor's price under the present structure, that is only because *it can't match their costs.*

3. The Need To Strengthen The Postal Rate Commission

A related but also necessary step to restoring the financial soundness of the Postal Service is to give the Postal Rate Commission the tools necessary to effectively regulate the Postal Service. If nothing else, the experience of the past 25 years has taught us that the currently restricted powers of the Rate Commission are simply inadequate to allow it, despite the best of intentions, to adequately protect monopoly ratepayers and preserve competition.

Despite the fact that it possesses statutory monopolies on the delivery of letter mail and use of the mailbox, the USPS may (1) set its own revenue requirement[12] and (2) propose, and to an unprecedented extent, establish rates to recover its revenue requirement, both with a minimum of oversight from the Postal Rate Commission. Even when a Postal Service rate or classification proposal is before the PRC, the PRC may not compel the Postal Service to produce data necessary to properly evaluate the USPS proposal under the factors set forth in the Postal Reorganization Act. This situation is intolerable and is responsible for much of the delay in postal rate and classification proceedings. It should be rectified, for the current situation makes the USPS a statutorily entrenched monopoly subject to public regulation that is more cosmetic than real.

Unfortunately, the lack of any reasonable market or regulatory cost constraint leaves the Postal Service free to incur costs and invest in mail processing and delivery technology and methods which do not necessarily minimize the cost of performing its core monopoly functions.[13] Instead, the Postal Service has an incentive to over-invest in common (or shared) mail processing and delivery technology and methods to the extent that any cost reductions such investments yield for the monopoly service are less than the common costs that are allocated to the monopoly service.[14] Under the USPS' present cost allocation methodology, it is reasonable to conclude that this condition is almost always satisfied.

Regulatory agencies statutorily charged with the oversight of firms with these incentives generally are afforded certain regulatory powers necessary to protect the public from the abuses of market power. While the Postal Rate Commission is charged with similar responsibilities, it was not provided adequate tools to meet these obligations. The necessary regulatory tools include the authority to: (1) issue final rate and classification decisions, (2) subpoena from the Postal Service necessary data.

C. Avoid Market Distortions And Protect Ratepayers By Ensuring That Postal Rates Minimize Competition with the Private Sector.

A modern Postal Service should ensure that price structures protect ratepayers, competitive markets, and avoid downstream market distortions. Government competition with the private sector is *not* something this Committee should affirmatively seek to increase.

The Postal Service's increasing efforts to divert scarce resources from core postal functions by adding new products to enter competitive markets or expand volume for certain existing services are harmful to both the economy and its captive mailers. The Postal Service's ill-fated "Neighborhood Mail" experiment is an example of the former; the new "Enhanced Carrier Route" subclass is an example of the latter. The Postal Service's "Neighborhood Mail" service would have placed the Postal Service in direct competition with list companies, saturation mailers and newspapers. In the aftermath of the firestorm of opposition that erupted upon the Postal Service's announcement of the service—most of which came from direct mailers and *not* from newspapers[15]—the "Neighborhood Mail" experiment was quickly and wisely aban-

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[12] The ability to set its own revenue requirement gives the Postal Service the ability to provide service at whatever cost level it desires; the Postal Service has absolutely no incentive to minimize costs. One way to solve this problem is to give the PRC the authority to set the revenue requirement.

[13] Giving the PRC the ability to set the revenue requirement would provide incentives for USPS to control costs.

[14] *See* Braeutigam and Panzer, "Diversification Incentives Under "Price-Based" and "Cost-Based" Regulation," Rand Journal of Economics. Vol. 20, No. 3, at 382 (1989).

[15] The tone of the complaints from the direct mailers at that time closely reflected many of the concerns in this Statement. Yet, those concerns seemed to have faded now that the competitive energies of the Postal Service are directed away from the direct mailers. Before endorsing "competitive pricing flexibility" the direct mail industry may want to consider long and hard

doned. The "Enhanced Carrier" subclass is harmful to captive mailers because it sets the scene to unjustifiably and uneconomically shift costs onto them.

To prevent the competitive harm and burden on ratepayers which would result from these activities, the Postal Service should be required to set prices in a manner which avoids harm to competitors and avoids distorting competitive markets. Simply put, in the absence of market failure, government provision of services is unnecessary and wasteful. Similarly, where provision of services by government entities is deemed expedient, the government must take steps to assiduously avoid harming ratepayers and competitors or distorting competitive markets.

Two fundamental changes in the approach to postal regulation are required to minimize the impact of postal pricing on competition and First-Class ratepayers.

First, a modern Postal Service should minimize competition with private sector firms. Congress should clarify that postal rates should be set in a manner that minimizes Postal Service competition with private sector firms and interference with private sector markets.

Second, a modern Postal Service should not be allowed to set postal rates in a manner that harms captive monopoly ratepayers. This can be achieved by ensuring that the Postal Rate Commission assigns institutional costs in order to ensure that rates are set in a manner consistent with the "First Principles"—universal, nondiscriminatory service—described above. At present, the total institutional cost pool of approximately $18 billion[16] is allocated by the Postal Rate Commission in the process of generating its statutorily required rate recommendation. At present, some 76 percent of institutional costs are allocated to First-Class, even though First-Class accounts for only 54 percent of volume. This disparity must be redressed.

Some have argued that the Commission must place greater weight on "demand" or Ramsey pricing in setting rates, particularly through greater use of what economists call the "inverse elasticity rule (IER)." Although postal rates were once set in such a manner, as the Commission acquired more experience and practical expertise it began to move away from the use of such blunt, rote calculations. This move is a commendable one and, indeed, the Commission has properly rejected pleas in recent cases that it place more weight on IER pricing approaches.

One of the biggest problems with IER or "demand" pricing is that it results in placing the heaviest institutional cost burden on those mailers held captive by the Private Express Statutes. This is true because, due to the Private Express Statutes, they have the most "inelastic" demand. The perversity and unfairness of this approach is patent: individuals and businesses forced to use First-Class mail because of the Private Express Statutes are losers under IER precisely *because* they are legal captives of the USPS. It is grotesque to suggest, as some do, that "demand" pricing is more "efficient" when the Private Express Statutes so distort the market. Indeed, utilization of inverse elasticity pricing by the Postal Service has been roundly criticized by eminent economists.[17]

Although the Rate Commission has, in recent cases, made some attempts to rectify this unfairness, we agree with the Commission that there remains much room for improvement in this regard. Unfortunately, *every single rate proposal* by the Postal Service over the past decade would have made matters even worse, as the USPS has repeatedly tried to shift even *more* of the overhead costs onto the already heavily burdened First-Class mailer. It, and the large mailers in other classes who stand to benefit, have supported these efforts by advocating greater use of IER pricing.

The only way to put an end to these persistent efforts by the Postal Service and the larger special interest mailers is to state plainly that postal rates should be based more on the basic principles of protecting captive ratepayers and promoting universal service.

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whether it thinks its backroom lobbying forces at Postal Service Headquarters—which are substantial—can forever shield the direct mail industry from the abusive behavior that "competitive pricing flexibility" would unleash. Many direct mailers, after all, provide essentially "middleman" services, and a "competitive" Postal Service, unchecked by either regulation or market forces, would have the incentive, opportunity, and ability to eliminate the middle man, and pick up those profits for itself.

[16] Per rate case R94–1.

[17] *See, e.g.,* William B. Tye, *The Postal Service: Economics Made Simplistic,* 3 Journal of Policy Analysis & Management 62 (1983); Frank A. Scott, Jr., *The Pricing Policy of the Postal Service: Economics Misapplied,* 4 Journal of Policy Analysis & Management 251 (1985); William B. Tye, *The Pricing Policy of the Postal Service: Policymaking Misunderstood,* 4 Journal of Policy Analysis & Management 256 (1985).

CONCLUSION

The Postal Service is at a crossroads. Unfortunately, it has chosen a course that is inconsistent with its mission and harmful to the larger interests of the nation, as it seeks to interject its monopoly power into competitive markets to the detriment of burdened ratepayers. In light of these problems, it is appropriate and necessary for the Congress to give the Postal Service direction that will guide it down the right path for its future. The primary tenets of this direction should include the preservation of high quality universal service at nationwide rates, restoring the financial soundness of the Postal Service, and minimizing the effect of the Postal Service on competitive private enterprise.

Chairman STEVENS. Thank you all very much. I'm sorry it has been broken up. I look forward to seeing you. We will have another hearing Monday afternoon.

[Whereupon, at 12:24 p.m. the hearing was adjourned subject to the call of the Chair.]

UNITED STATES POSTAL SERVICE REFORM: CONVERSATIONS WITH CUSTOMERS

MONDAY, MARCH 18, 1996

U.S. SENATE,
SUBCOMMITTEE ON POST OFFICE AND CIVIL SERVICE,
OF THE COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2:07 p.m., in room SD–342, Dirksen Senate Office Building, Hon. Ted Stevens, Chairman of the Subcommittee, presiding.

Present: Senator Stevens.

OPENING STATEMENT OF SENATOR STEVENS

Chairman STEVENS. I am sorry to be slightly late. We want to continue this afternoon the hearing on Postal Service Reform. This is a continuation of what we call Conversations with Customers, which we began on Thursday of last week. Our interest really is in hearing from the mailers themselves for your suggestions for steps to modernize the Postal Service.

We are going to hear from a new group in the postal community, the Main Street Coalition for Postal Fairness, and from the National Federation of Nonprofits. Because of a scheduling change, the Alliance of Nonprofit Mailers is not going to join us today, but has provided testimony for the record.

[The statement referred to follows:]

PREPARED STATEMENT OF NEAL DENTON, EXECUTIVE DIRECTOR, THE ALLIANCE OF NONPROFIT MAILERS

Mr. Chairman, the members of this large coalition of nonprofit organizations appreciate the opportunity to join with other customers of the U.S. Postal Service in testifying before your Subcommittee. We are confident the record that you are compiling, along with that of your colleagues in the House, will assist in crafting meaningful reforms to the Postal Reorganization Act.

But frankly, from our point of view, legislative reforms need not involve any "dramatic overhaul," as some may suggest. Postal Service management and the Board of Governors do need to redouble their efforts with respect to automation and further improvements in the infrastructure of our national delivery network, but we don't believe the Postal Service is "broken." It is from that perspective that we make these comments today.

The Postal Service is the only machinery of government that touches each of our lives six days a week. It's core job is to accept hard copy mail—greeting cards, newspapers, advertisements, bills, fundraising appeals, journals and parcels—from senders and to deliver it to recipients. As customers and consumers, we ask that delivery be prompt, be reliable and be priced fairly.

Hard copy mail has been around for centuries, and it is not about to go away. The Postal Service is a $55 billion operation delivering over 180 billion pieces of mail annually. And each year the volume of mail increases. When asked what our vision of the USPS will be in five years, or in ten years, we can only hope that the

USPS, led by strong management and a thoughtful Board of Governors, will still be focused on its core mission and dedicated to providing delivery service that each year becomes more prompt, more reliable and less expensive. Were the Postal Service to accomplish this, and only this, I suggest that many of its perceived problems would rapidly fall by the wayside.

It is true that the Postal Service has lost considerable precious time in introducing high-speed postal automation into this decade. I will not belabor here the length of time or the amount of money that the Postal Service has required for its initial automation efforts. Suffice it to say that a modicum of automation is at last operational in some of our postal facilities. But, to use a baseball metaphor, the Postal Service has barely gotten to first base.

USPS sorting of flats and parcels, internal materials and handling methods, and accountability via the ability to track and trace shipments are all quite primitive. The opportunities for improving the national mail delivery network are both obvious and seemingly endless . . . but will come at a cost. In order to improve automation capabilities, the Postal Service will be required to invest additional significant expenditures for new plants and equipment. In this area, Congress may want to review the $2 billion annual borrowing limitation for capital improvements contained in the Act.

There are some who suggest that the USPS should be our doorkeeper to modern technology and that the Postal Service should create product lines that would safeguard E-Mail transmissions or take an active role in America's fascination with electronic communications. Considering that the Postal Service still finds wooden pallets to be a relatively new technology and the use of bar codes to be revolutionary, I recommend that we be more than a bit skeptical.

The impressive infrastructure built for the collection, sortation, transportation and delivery of mail does not seem to lend itself to the fast-paced technological changes that lie ahead in the electronic communications industry. Besides, the Postal Service has already lost precious time in bringing high-speed postal automation into this decade. Automated sorters, readers, and feeders are long overdue in many postal facilities around the country. Is expensive research and development of potential online services for electronic communications a justifiable use of the money that postal ratepayers contribute to the Postal Service?

All of this talk of "securing" electronic mail safety via some sort of USPS vehicle seems even more out of place considering the Postmaster General's recent musing about abandoning some of the Postal Services more core functions.

It is our recommendation that the Postal Service stick to its knitting and not plunge into new ventures using postal rate revenue to compete in a market that already has many well-established alternatives. Those explorations are better left to others.

I would suggest instead that the USPS let the Congress decide how best to monitor and regulate that new frontier. If the USPS can feasibly provide such a service *and* Congress determines that activity fits into an expanded USPS charter—and it does not detract from the USPS focus on mail delivery—we'll be sold.

The name of the Postal Service's game is mail collections and delivery; and it is the responsibility of the Board of Governors to keep their eye on the ball—and to be certain that management's eye doesn't wander too far away.

So, what new tools, what new power can the U.S. Congress grant to the Board of Governors of the U.S. Postal Service to assist in this responsibility of collecting and delivering the mail? I'm sure you've heard some good ideas in these hearings, and you've heard some questionable ideas. After everyone has exhausted their "wish lists," I would also suggest that one of the most simple and effective is to add some accountability to the Board of Governors.

Currently, the only party at USPS Headquarters that can openly question the policies of senior management without fear of retribution is the Chief Inspector of the Postal Service. I've come to understand that some of the Governors seek out the counsel of the Chief Inspector at times because they appreciate his frank assessment of matters.

Even though USPS management (and perhaps some Governors) will oppose this new tool, I suggest that the Board of Governors should be afforded with a small, but learned and effective full-time staff similar to that employed by the Postal Rate Commission. If the funding and staffing of that body were kept separate from USPS management staff, I believe the quality of decisions and oversight generated by the Governors would improve.

Perhaps some of us "skeptics" would be inclined to support ideas giving the USPS more flexibility on pricing and product development if proposals were scrutinized by a professional staff with the insulated ability to question management.

It is the responsibility of Postal Service management to address the needs of their customers. It is the responsibility of the Board of Governors, as appointed by the President with Senate approval, to oversee postal management and to guard over the general interests of the public. Recently, some have questioned their effectiveness. Former Postmaster General Anthony Frank even suggested that this "supine" body is "not a factor in the Postal Service." That alarms me because it comes from such a respected figure in recent postal history—and because it might well be true.

Increase the pay of Governors if necessary, increase the pay of senior management as senior management suggests, but leave enough to add a competent and separate staff for the Board of Governors. I believe that might be the best new tool that we can give to the Governors of the U.S. Postal Service if we are to really begin to improve the national mail delivery network in the country.

The Postal Service wants flexibility to set prices. With the USPS's track record, this is an uncomfortable proposition. We should consider caution before granting a government-protected, monopolistic entity the unilateral authority to set its own prices. In the 1994 rate case the USPS proposed rate increases of 34 percent for community newspapers. Only through the current process of adjudicating these proceeding before an independent Postal Rate Commission was the Postal Service found in error and the proposed rates that would have seriously overcharged those community newspapers was reversed.

In the same proceeding, the Postal Service increased the postal rates to our local libraries by 71 percent. The Postal Rate Commission, while frustrated because the Postal Service was not providing adequate data, accepted the increase but warned that it was likely in error. Facts have shown that the Postal Service was indeed wrong. The overcharge to America's libraries is substantial—and yet the Postal Service refuses to correct the problem.

Requests for price flexibility would be better received if Postal Service management and the Board of Governors showed good faith when mailers are so obviously overcharged.

The current ratesetting process could use some changes. It does take too long and it is too expensive for mailers to adequately participate. Although the USPS is leading the charge in criticizing the current process, the USPS should also shoulder much of the blame—it very often does not provide adequate data to the Postal Rate Commission. When the process begins with incomplete or faulty data, the end product is likely to contain errors or unfair rate prejudices. If you can glean some suggestions from these panels that will improve that process without dismantling it, we would be most supportive.

To be frank, our coalition hasn't found much in recent PRC decisions to be very happy about. However, given the choice, we would rather place our trust in an independent body that is responsible to America's citizenry to make important postal rate decisions.

In closing, we all know that there are always "special interests" tugging at every governmental body. Produce shippers would like the USPS to offer refrigerated mail trucks; producers of valuable articles would like the USPS to offer overnight service for highly-insured shipments; most mailers would like the USPS to better track mail delivery time; smaller, single-piece mailers want to keep stamp prices low; postal labor wants better wages and working conditions, and America's volunteer and charitable community would like better treatment for nonprofit mailers.

As you and your colleagues in the House continue to deliberate on how best to improve the United States Postal Service we trust that your focus will remain upon the core mission of moving this nation's mail quickly, efficiently and at the lowest cost possible.

Chairman STEVENS. We have reviewed the written testimony from the witnesses. As a matter of fact, I have just returned from Alaska and I took some of them with me over the weekend. I would urge that you summarize your statements and proceed as you wish. I don't know if any other Members are going to join us today, but I hope so.

Representing the Main Street Coalition for Postal Fairness is the newly named Executive Director, Jack Estes, accompanied by Guy Wendler. I understand you are representing the American Business Press—is that right—as a member of the coalition?

Mr. WENDLER. Yes.

Chairman STEVENS. Also, we have Lee Cassidy, the executive director of the National Federation of Nonprofits.

I welcome you, gentlemen. I have asked you to join in sort of a panel expressing your points of view. We do hope that we can have an exchange as you testify, and I hope to be able to finish this portion of our procedure and get around now to drafting a bill. By the end of this week or the middle of next week, we hope to have a draft bill and start talking to other Members of the Committee. So it is very important that you do give us your views today, and I want to welcome each of you and thank you for taking the time to come. I thank you for being willing to change the date. There was a problem of a collision with another committee last week.

Mr. Estes, if you would proceed first, we would be pleased to have your comments.

TESTIMONY OF JOHN T. ESTES, EXECUTIVE DIRECTOR, MAIN STREET COALITION FOR POSTAL FAIRNESS

Mr. ESTES. Thank you, Mr. Chairman. It is a pleasure to be here and we want to thank you very much. Primarily, we are appreciative of being able to sit at this table before you because, as you point out, we are a new team, but I want to express to you the fact that although we are new, our players all have a great deal of game experience. We are a cross-class group of mailers engaged heavily in first-, second- and third-class. We are largely small and medium-size businesses who depend extensively on the Postal Service. Because of that, our postal costs represent a significant amount of business expense for us.

Our coalition mission is set forth In Exhibit B of our statement. Exhibit A gives our members. I won't go through that mission statement other than just to summarize it for you by saying that our mission is largely to preserve a cost-efficient Postal Service and universal rates and universal service and a strong, effective Postal Rate Commission.

The coalition supports modernization of the Postal Service, Mr. Chairman, but the new Postal Service, in our judgment, must continue to strive to provide fair and effective service. Our coalition stated because this is a critical time for the Postal Service, it also now presents a great opportunity to both preserve and improve one of the most needed public services in our country.

A number of points have been made in our statement. I won't go through them. Many of the buttons that we have touched on in our statement have been touched on by others in appearances before you, but I would like to make three points, one we believe to be very critical and the other two highly significant.

As to the first critical point, Mr. Chairman, you know that very often substance is often determined by procedure. One can take various sides of whether or not that is a good or a bad practice, but unfortunately frequently it is the truth. Because the Postal Service reform issue is a momentous problem for one of the most complex institutions in our society—it is occurring at a time of a fast-changing culture with rapidly evolving technological innovations—because of that background, Mr. Chairman, we submit to you that it is imperative that Congress receive the most reliable, the best tar-

geted and the best focused advice that can be mustered to guide it in this highly important function.

Therefore, our suggestion, Mr. Chairman, is that we urge you to appoint a congressionally-approved reform commission to explore all aspects of what the Postal Service should be, how it should be modernized, and how it should be reformed. This is not, Mr. Chairman, just a jump-start effort. This is not a suggestion that we tinker around the edges of the Postal Service. It is a hope that you will seriously consider and we will give you some thoughts, if you would like, on the best way to proceed so that we can bring the mailing community—the other stakeholders in this problem can bring to you the very best advice that can be mustered.

We would hope that if this is done that it should be done in a manner which strives to build a consensus, a commission that is appointed with men and women that have highly effective public interest at heart. We would hope that the vested interests which most mailers have could be put in the background so that we can receive and give to you the very best advice possible.

We would hope that there would be targeted assignments with firm completion dates. We would anticipate that this commission would report back to you at a date certain specific recommendations so that, if not in this Congress, early in the next Congress you, the Congress, would be prepared to receive and would receive the very best advice that we can muster.

There are matters that need to be resolved and which, if you find merit in this suggestion, and we earnestly hope you do, can be reviewed, matters such as who would appoint the commission, how to develop an agenda, how should it be financed, what is its standing now and in the next Congress—even though the Senate as a continuing body may not have that much of a problem, to some extent we may in the House—and the completion deadlines.

So the critical, the most important, the earnest plea that we make to you is that you seriously consider this suggestion and that we all roll up our sleeves and bring to the Congress the very best from this community that we can on this highly complex and very important mission.

Second, Mr. Chairman, as to some other remarks that I just wanted to make—and it may be that if you do find merit in the commission reform proposal that these things could be folded into that effort, but we believe that it is very important that the Postal Rate Commission, as you have heard before, not only be continued, Mr. Chairman, but it also be materially strengthened.

We have proposed in our statement four changes which we think are germane to the functioning of the Postal Rate Commission. Briefly, they are final decision authority in rate cases; reducing from 10 to 8.5 months the decision time as a consideration; subpoena authority so it can receive promptly the needed advice, data and material that is required from the Postal Service; and standing to represent itself in courts of appeals. I know you will find these familiar, Mr. Chairman, because in the spring of 1991 they were your ideas which at that time were introduced. We think that given the lapse of time since you introduced those ideas that even more so now they are relevant and germane and should be considered.

As you know, of course, the Postal Service, on the other hand, wants less regulatory oversight and less regulatory involvement and freedom, in their view, to intervene more precisely and quickly in the marketplace. That raises the third issue that we would like to just briefly mention to you, and that is what are the activities of the Postal Service, what should it do, how it should be crafted and how should it be controlled or not.

We have included in our statement, given the fact of the current uncertainty and ambiguity and confusion that has, we believe, developed with respect to what activities, particularly in new businesses, the Postal Service should or should not be engaged in, that we reaffirm specifically that the purpose, the mission and the legislative thrust of the Postal Service is to provide universal service at universal rates.

At the bottom of page 5 of our statement, we have included also a notation from the 1970 Senate report that accompanied the 1970 Postal Reform Act, and as you will see, those two lines read, "That the Postal Service is in fact and shall be operated as a service to the American people, not as a business enterprise, designed to provide excellent postal service . . ." We would encourage that the Committee reaffirm that basic 1970 statement.

Also, on the next page there are several other interesting observations that the report made in accompanying the 1970 Act. But it should be clearly resolved what market activities shall the Postal Service be permitted to engage in, and it is important to remember in that resolution that the Postal Service is, of course, a public monopoly.

In conclusion, then, Mr. Chairman, we believe that the Committee should be specific and precise on Postal Service permissible ventures. We believe that the administrative and enforcement powers of the Postal Rate Commission should be enacted, and we earnestly urge you to consider appointing a commission to bring before you and the other Members the very best advice that we can.

We think that this will assist in building a consensus. We hope that it will ease the way for modernization and effective reforms, and we believe, as you know, that it is critical because time is so short, not only in this Congress, but because of the ongoing activities and the need of the Postal Service to receive and for you to receive the best advice that we can prepare.

Thanks, Mr. Chairman.

Chairman STEVENS. Thank you.

[The prepared statement of Mr. Estes follows:]

PREPARED STATEMENT OF JOHN T. ESTES

Chairman Stevens and Members of the Subcommittee: Thank-you for inviting our Coalition to appear before you today and allowing us to offer testimony and express our views on a matter of major public policy significance. It is our desire to be a helpful and constructive participant throughout this process and particularly during this second series of your hearings: "USPS Reform-Conversations with Customers." As requested in your invitation we will address how we feel about the future of the Postal Service, our vision of the USPS in the future, how that vision can become a reality and offer for your consideration specific steps that could be promptly initiated to get the ball rolling on a Postal Service modernization process.

About the Main Street Coalition

Our coalition consists of mailers including relatively small business mailers and mid-to-smaller circulation publications whose interests and operations are heavily

impacted by the policies of the Postal Service. In the Postal Service of today, operational practices and rates seem increasingly dominated by large volume mailers. We believe our view and more importantly our needs are often not heard—that is until you kindly extended this invitation. We believe our concerns are frequently drowned out by the constant drum beat of Postal Service pleas for bigger market shares, pricing flexibility, relaxed regulatory oversight by the Postal Rate Commission and an alleged inability by the Postal Service to compete effectively with private sector providers of various types of delivery services. We readily admit that some of these Postal Service complaints might very well have merit, but we want to raise with you today the prospect that this might not be such a bad result from a public policy standpoint. In other words we want to share with you "the rest of the story."

Our coalition is in a growing and formative stage and as of the end of last week consisted of those organizations listed and described on the attached Exhibit A. These organizations have adopted mission statement which is contained on Exhibit B.

Four Basic Points

At the outset, Mr. Chairman we wish to make for you and the Committee today the following four basic points:

First: The Postal Service is one of the most if not the most complex institutions in the country. By design it maintains a delivery and transportation system to which everyone, as a matter of right has access for both home and business delivery services. The sheer magnitude of the Postal operation and its omnipresence frequently in nearly every facet of our daily activities demands that any modernization or reform proposals be not only carefully crafted, but evaluated from a large number of public policy considerations

Second: Any modernization or upgrading of the Postal Service (a process from which we do not shrink and indeed support with enthusiasm) must under no circumstances place in jeopardy universal service at universal rates. These are the linchpins of the Postal Service. Mailers have a simple request: Deliver the mail in an efficient, cost effective, and reliable manner to every address in the nation. Although our needs may be simple, we confess that their fulfillment may at times be complex and difficult resulting in the requirement to either fine tune or modify the delivery mechanism.

Third: Any substantive Postal Service modernization program or reform proposals must at a minimum address the following key areas:

(A) *Rate making:* Improving the effectiveness of the Postal Rate Commission.

(B) *Labor reform:* Meaningful labor-management collective bargaining process changes and other employee relations policy improvements aimed at encouraging voluntary dispute settlements, discouraging adversarial arbitration proceedings and encouraging work floor assignment flexibility and incentive compensation awards for superior performance.

(C) *New postal products:* Controlling the entry into new product ventures by defining the core mission of the Postal Service so that fulfillment of its public service obligation is never compromised by competitive participation in projects performed in the private sector.

Fourth: The process by which any modernization or reform proposals are developed is a crucial step. We propose that a Congressional Commission be established for this purpose. In our view a thorough review of some or all of the Postal Service activities is an undertaking of such significance and magnitude that it should be the product of a bipartisan, multi-skilled, broadly based combination of experienced, informed and knowledgeable individuals. We would recommend the Commission include those with postal management and regulatory backgrounds as well as those with labor and financial experience. In addition to business management experience the Commission should include someone with knowledge of advanced postal and industrial automation procedures as well as customers who utilize the various classes of service and impartial and knowledgeable members of the public. The Commission should be assigned specific projects with firm completion deadlines for reporting back to the Congress their recommendations. We feel very strongly about this approach because it is essential that there be a consensus building effort involving broad participation of stakeholders with a vested interest and others with impartial views. Every effort should be made to select those capable of putting aside any attitude of hostility and acrimony. Where recommendations on Postal Reform cannot be

reached after good faith review and analysis, the Congress should expect to receive clearly defined options from the commission.

Elements of the Post Office of the Future

You have requested our views of the Postal Service of the future. Set forth below is a partial "wish list" for such an organization indicating where possible what we believe are required departures from existing policies and practices:

Cost Control

The Postal Service in the 21st century must be one that has a firm grip on controlling its cost of operations. Costs must be brought under control and not allowed to continue to soar out of control. Automation programs must result in a decrease in work hours rather than as now in an increase.

The primary problem facing USPS today is the continuing increase in costs in the face of massive investments in automation and large volumes of work shared mail that ought to reduce costs. Instead, the number of work hours and employees continue to grow, even when volumes of some classes are relatively stagnant. While a 1992 downsizing cut career employment by about 50,000 positions, career employment now exceeds the level achieved before the reductions.

Labor Reform

Changes must be made in the management of labor management relations resulting in fewer grievances and more frequent settlement of disputes by negotiation rather than by arbitration. The spiral in deteriorating union relations will be abated through intensified efforts at communication and joint management-labor involvement in employee relations.

Postal Service Mission

The statutory mandate of the Postal Service should continue to be universal mail service at universal rates[1] which will remain in place as the primary purpose of the Postal Service. The USPS will be viewed as a service and not a business. The basic functions of the USPS as described in the 1970 Senate Report accompanying the Postal Reorganization Act, will remain as follows:

> That the Postal Service is in fact and shall be operated as a service to the American people, not as a business enterprise, designed to provide excellent postal service;
>
> That the Postal Service achieve and maintain compensation for its employees comparable to that of the private sector of the U.S. economy;
>
> That the postal rates and costs be apportioned fairly and equitably among all users of the mail;
>
> That letter mail be sealed against inspection and always be delivered with priority;
>
> That transportation be modernized and designed to achieve the most expeditious delivery of mail possible; and
>
> That postal facilities be designed to improve the service, to provide convenience for the public, and to have ready access to air and surface transportation facilities.

Please note the USPS was not intended to be a "business enterprise," occasional statements by current postal management notwithstanding, nor should it be. It is a tax exempt public monopoly, complete with its own police force, that fulfills a constitutional obligation to "bind the nation together".

More than one-third of the total costs of the Postal Service are institutional costs—i.e. fixed costs that are the price of a universal postal system that existed long before mass direct mail advertising, express mail, or bar coded envelopes. USPS is not a business, it is a public service delivery system that can and should be managed more efficiently, employing many of the techniques U.S. business has had to adopt to increase productivity and improve customer service. But the goal of USPS is not to profit shareholder; the goal is to maintain a national universal postal network available at the lowest, most reasonable rates to all users, all of whom benefit from the existence of a universal system.

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[1] Central to these concepts are non-discriminatory rate schedules available to all mailers, adopted in an open public proceeding and not negotiated between two parties without regard to the impact on other interested parties.

A "business" would not have uniform rate schedules for letters and books across a continent, and it would not deliver parcels to the mountainous counties of West Virginia, the Alaskan bush, the apartments of the poorest urban constituencies, the mailboxes of farms far away or the shores of the Virgin Islands, at the rates charged by USPS, nor would it staff postal facilities in those localities.

Rate Making

The Postal Rate Commission should have final decision authority in rate proceedings, very possibly have a reduced maximum of 8½ months or 265 days to issue its decisions, possess subpoena authority to obtain information from the Postal Service and have standing as a party in any appellate proceeding involving one of its actions. I am sure Mr. Chairman these are familiar to you, as they are the bills you introduced in the Spring of 1991 and are even more appropriate today after several more years of evaluating the current rate making process.

In our view the Postal Rate Commission is one of the great successes of the Postal Reorganization Act, but that is rarely stated. Its current 10-month maximum window on handling massive billion dollar rate cases requires it to move at the speed of light compared with other regulatory bodies. The Commission, as you know, just completed in 10 months an extremely complex classification case that involved major changes in all classes that will have an impact on mailers, printers, fulfillment bureaus and letter shops employing thousands of people. Appropriately, everyone had a place at the table involving those far reaching changes and billions of dollars. We nevertheless agree that your 1991 proposal to reduce the decision time, coupled with the safeguards contained in that proposal, requires serious consideration.

We believe that smaller mailers must rely on a universal system of rates established by the Postal Rate Commission, which has no self interest in inflating any one customer's volumes. These rates are the result of a careful balance of costs, market, and policy factors Congress wisely required be considered. Understandably there is controversy about who pays the greatest share of institutional costs incurred to benefit all mailers.

The PRC has unfairly borne criticism for doing what it is supposed to do, i.e., assume the role of both an arbitrator of rate requests and a rate expert, functions that Congress had performed before 1970.

As you know Mr. Chairman, the USPS not infrequently presents the Commission with controversial proposals that major segments of the mailing community oppose. The Commission has done its job and fulfilled its responsibility by adjudicating fairly among these competing interests. We are particularly appreciative to the custom at the PRC to carefully consider the smaller mailer whether an individual or a small business and weigh potential injury from severe rate increases. The small mailer needs the PRC, Mr. Chairman. There is frequently no place else to turn because the immense bargaining power of a Readers Digest, L.L.Bean or Time-Warner is not available when dealing with the USPS. We find it ironic that the primary legislative proposals that have been publicly floated this year to restructure USPS consist mainly of proposals that would diminish the independence and the authority of the Postal Rate Commission.

Where Do We Go From Here

The Postal Reorganization Act of 1970 has been an overall success: end of congressional subsidy practices, automation in mail processing, mailer presortation, vast increases in first and third class volumes unforeseen in 1970, modernized postal facilities, great strides in improving workplace safety and facilities. We applaud the thousands of dedicated postal employees and their predecessors who deserve recognition for managing the mammoth enterprise as well as they have and for dealing with obstacles unforeseen in 1970 (e.g., billions in imposed health and retirement assessments mandated by Congress).

Mr. Chairman, precipitous legislation will not solve problems that are caused by forces and events that are not thoroughly understood. We need the Postal Reform Commission that is recommended above and now is the time to act. As you know there are not many legislative days remaining to get this program up and running. Your appreciation of the complexities involved in tackling this issue and the knowledge you have acquired throughout the years you have been involved with the postal industry, present an opportunity to act that we hope will not slip away. Furthermore, an immensely important, highly complex and potentially inflammatory issue will be removed from the partisan climate we are now entering and the careful, thoughtful and judicious evaluation so desperately required can get underway and results be available for Congressional review early next year.

This is our recommendation for action that can be taken now and move this issue off of dead center toward a meaningful resolution. We of course remain available to work with you and the Committee in any way that we can to accomplish this objective.

EXHIBIT A

THE MAIN STREET COALITION FOR POSTAL FAIRNESS

MEMBER INFORMATION

American Business Press (ABP) is a publishers association representing over 153 major publishing companies and approximately 850 trade and business periodicals. Its members are leaders in the business-to-business communications field. The business-to-business medium is a $5.5 billion industry that has become the predominant source of information and news among industry leaders.

The Coalition of Religious Press Associations (CRPA) includes the major Catholic, Jewish and Protestant press associations in the United States. Taken together, these associations represent over 1,200 United States periodicals. With few exceptions, CRPA use the Postal Service for distributing their magazines and newspapers to their subscribers.

The Greeting Card Association (GCA), a nationwide industry trade organization, was founded in 1941. It is an organization representing American and international greeting card publishers and others involved in the production and distribution of greeting cards at the wholesale level. The greeting card industry contributes almost $7 billion in retail sales each year to the economy and two-thirds of the 7.4 billion greeting cards sold each year are sent through the mail.

The National Federation of Nonprofits is a coalition whose purpose is to assure affordable postage rates, efficient postal service operations and fair regulation for its constituency. Membership in the Federation includes several hundred organizations with greatly varied nonprofit purposes: humanitarian, educational, cultural, religious, health and fraternal.

The Newspaper Association of America (NAA) is a national trade association serving more than 1,500 member newspapers in the United States and Canada. NAA members account for more than 85% of the U.S. daily circulation. Roughly 60 percent of NAA's daily newspaper members are under 25,000 in circulation. NAA has been involved in postal issues for over a century and its Board has identified postal issues as the organization's top priority in the public policy arena.

Hallmark Cards Inc. is the world's leading manufacturer of greeting cards and related personal expression products. Hallmark serves more than 45,000 retail outlets domestically, including specialty, department and book stores as well as food, drug and general merchandise stores. Hallmark products are also available via online services, catalogs and software retailers. Worldwide sales in 1995 were $3.4 billion.

Knight-Ridder, Inc. is a major communications company which owns and operates 31 daily newspapers. Their papers serve approximately 2.8–3.5 million households daily and on Sunday many of which involve medium and small cities.

Penwell Publishing Co. is located in Tulsa, OK with offices in Nashua, NH and Houston, TX. Publications include *Oil and Gas Journal, Fire Engineering* and *Computer Graphics World.*

EXHIBIT B

THE MAIN STREET COALITION FOR POSTAL FAIRNESS

MISSION STATEMENT

- To protect a universal mail delivery system for both businesses and consumers with the primary goals of providing reliable and timely service at reasonable and nondiscriminatory rates.
- To support efforts to control costs, improve the productivity and efficiency of U.S. Postal Service management and operations and to ensure the continuation of the institution as a fundamental public service.

- To seek enhancement of the authority of the Postal Rate Commission as an independent body to review and rule on all proposed rate and classification changes.
- In light of the Postal Service's monopoly position, to oppose any efforts to (1) shift more overhead costs onto captive customers; or (2) give the Postal Service the ability to grant special rates and volume discounts to large mailers.

Chairman STEVENS. Mr. Wendler.

TESTIMONY OF GUY H. WENDLER, PRESIDENT, STAMATS COMMUNICATIONS, INC., ON BEHALF OF AMERICAN BUSINESS PRESS

Mr. WENDLER. Thank you, Mr. Chairman. My name is Guy Wendler and I am very grateful for the opportunity to express my views and those of the American Business Press today. It is exactly that opportunity to be heard and due process that we are interested in protecting.

The issue is whether Congress must or should legislate fundamental changes in the way the Postal Service and the Postal Rate Commission operate. Despite what you might hear from the Postal Service and others who stand to benefit, and even though there are areas where improvement can be made, the American Business Press believes that no such fundamental restructuring is either necessary or appropriate.

More than 850 magazines and trade newspapers belong to the ABP. They reach out to approximately 27 million readers and cover all parts of the country's professions, education, health care, government, and the business world in general. These ABP member magazines and newspapers keep our business leaders informed and contribute to the Nation's growth, its international competitiveness and its economic well-being.

As a publisher of relatively small-circulation magazines, I need the Postal Service. It is the only carrier that can deliver our magazines to our subscribers, and for that reason I would be more than concerned if I thought that the Postal Service's ability to provide universal service at reasonable rates was threatened by technology or other changes.

Of course, the Postal Service cannot remain static in the face of these changes, but that does not mean that a massive overhaul of the regulatory framework is appropriate. After all, the situation that exists today is a far cry from the situation faced by the Postal Service in the 1960's when ABP was a key advocate of postal reform. At that time, the Postal Service was plagued by work stoppages, deteriorating facilities, skyrocketing costs, and was propped up by hundreds of millions of dollars per year in subsidies.

As a result of the Postal Reorganization Act of 1970, politics have effectively been removed from the Postal Service, and through the establishment and operation of the Postal Rate Commission, all mailers are entitled to a fair hearing on postal rates.

We understand that the Postal Service wishes to be free from some, or even all of these regulatory oversight constraints it now faces, but the case it presents has been overstated, certainly with respect to the existence, or rather the non-existence of a competitive threat to second-class mail. Although at the fringes and almost

exclusively for service reasons there are some daily and weekly publications that use small amounts of alternate delivery, they are very few and far between. My company does not and really cannot use alternate delivery because it is simply not available, and the same is true for the vast majority of specialized business publications.

Yet, the Postal Service has claimed that it is losing market share even in the publications field, a statement that is simply incorrect, as confirmed in the recent Postal Rate Commission hearings. In fact, the Postmaster General has recently gloated over having put Publishers Express, one of its very few competitors, out of business. So diversion of printed periodical mail is really a non-issue, and in the business publications field where I operate the same is true for diversion to electronic format, which is typically a supplement to and not a substitute for the printed publications.

We are, however, concerned about the potential economic impact upon the Postal Service of diversion of first-class mail to electronic format. This problem, however, cannot be addressed by shortening Postal Rate Commission proceedings or providing regulatory-free pricing power to the Postal Service.

The plain truth is that electronic media and communication will continue to grow regardless of what happens here, and it is for that reason that ABP submits the appropriate response should be for the Postal Service to improve its service, cut costs, increase productivity and efficiency, and in all respects perform better than it ever has in the past. It must put an end to labor costs that seem to escalate irrespective of flat or even declining mail volumes, and the flexibility it should be seeking is flexibility to manage its workforce and its contracting-out procedures in such a way as to minimize the costs of moving the mail.

One area where the Postal Service has appropriately placed emphasis, but perhaps not enough, is automation. My publication, *Buildings Magazine,* like most of those published by ABP members, is bar-coded, which saves the Postal Service and mailers several cents per copy. Unfortunately, even though the Postal Service governors stated in their March 4, 1996, that bar-coded mail produced by customers is essential to the success of the Postal Service's automation program, the Postal Service has yet to deploy flat sorting machines that can handle tabloid-size publications and newspapers, of which there are billions of mailed copies per year. This is an example.

We understand that the equipment does exist to perform automated sortation of periodicals larger than standard size which will save the Postal Service the manual sortation costs, but for reasons we don't quite understand, deployment is extremely slow and not expected to get much faster. Here is one way for the Postal Service to improve efficiency, lower costs and lower rates, totally apart from the Postal Rate Commission, and urge you to urge the Postal Service to get on with these types of cost-saving actions.

Automation and productivity increases are essential to the future of the Postal Service. Weakening or even eliminating the role in postal rate-setting now performed by the Postal Rate Commission is not. I know that some argue that the Postal Rate Commission

proceedings are too slow and that its role prevents the kind or pricing power the Postal Service wants.

However, as long as the Postal Service has a monopoly by law or in fact over most of this Nation's mail and tens of billions of dollars of revenues, and as long as only the very largest of mailers, the big guys, receive a sympathetic audience at Postal Service headquarters, it is essential that an independent Postal Rate Commission provide assurances that the policies of the Postal Reorganization Act make their way into rates and provide opportunities for all mailers, large and small, to participate in the rate-setting process.

I testified in the reclassification case and I know that my views and those of more than 100 other witnesses were heard and considered by the Postal Rate Commission. I have no confidence that my views would be considered by a Postal Service authorized to set its rates unfettered by regulation.

In addition, as a participant in the most recent proceedings before the Postal Rate Commission, I have come to realize why these proceedings take 10 months from the filing until decision. While I suppose the process could be shortened marginally, there is no way to shorten it substantially while assuring the parties their rights to a full and fair hearing on the record.

Who knows if an 8-month period would really satisfy the Postal Service? Maybe in those relatively few areas where there truly is effective competition, such as express mail or parcel post, there might well be a way for Congress to grant the Postal Service limited ability to modify rates or expand upon the Postal Service's already existing power to engage in experimental services. But as long as the Postal Service continues to see phantom competition around every corner, as it does with second-class mail, care must be taken that the Postal Service be closely regulated in that regard. The Postal Service cannot be permitted to define the so-called competitive services itself, however.

We do not deny that, without any change, challenges lie ahead for the Postal Service and, as I hope I have stressed, my company and publishers everywhere absolutely depend upon the continuation of a strong, universal and reasonably priced postal system. Although ABP believes that more harm than good would flow from a loosening of the regulatory process to expand the rate-setting power of the Postal Service, even if the reverse were true, it should be obvious that the fundamental problems of poor service, increasing costs and diversion to electronic media will be largely unaffected by any such changes.

It is for these reasons that ABP supports the creation of an independent commission to accomplish what the Kappel Commission accomplished in the late 1960's: To investigate the core problems facing the future of the Postal Service and develop solutions to those problems. To be sure, such a commission would and should study rates and rate-making flexibility, but it should also study management techniques, like contracting out; analyze the Postal Service's automation program; address the highly problematic area of labor-management relations; and determine whether or not the Postal Service should expand its product line or even contract its operations in the face of electronic diversion.

We stress, however, that neither Congress nor this Committee should function in a crisis mode. There is no crisis today, as there possibly was in 1970. There are problems, and the solution to those problems can best be developed on the basis of inquiry with broad participation by all concerned. ABP would be pleased to work with the Subcommittee, the Postal Service and all other interested parties to develop the facts on which real solutions can be based.

Thank you for the opportunity to discuss these views, Mr. Chairman.

Chairman STEVENS. Thank you.

[The prepared statement of Mr. Wendler follows:]

PREPARED STATEMENT OF GUY H. WENDLER ON BEHALF OF AMERICAN BUSINESS PRESS

Mr. Chairman, my name is Guy Wendler and I am pleased to have the opportunity to express my views and those of the American Business Press on the issue of whether Congress must legislate fundamental changes in the way that the Postal Service and the Postal Rate Commission operate in order to permit the Postal Service to survive into the next century. Despite what you might hear from the Postal Service and others, and even though there are areas where improvement can be made, we believe that no such fundamental restructuring is either necessary or appropriate.

As a bit of background, the American Business Press is an association of the nation's leading trade, professional, and specialized business periodicals. My own company, Stamats Communication, Inc., is a small family-owned and operated publishing and marketing communications company based in Cedar Rapids, Iowa. We publish newsletters, directories and two specialized business magazines, including *Buildings* magazine, which covers the construction, management, and operation of commercial, institutional, and governmental buildings. *Buildings'* monthly circulation is 46,200. We are also engaged, as are many other ABP members, in electronic media, producing CD-ROMS, internet services, and other computer-based media for colleges and universities and other professional organizations.

Among the other members of the American Business Press are Crain Communications, publisher of *Advertising Age* and *Automotive News;* Cahners Publishing Company, which publishes a variety of titles, including *Professional Builder, Variety,* and *EDN;* McGraw-Hill, which publishes *Aviation Week & Space Technology* and many other well-known magazines; BPI Communications, publisher of *Billboard* and *Architecture;* Compass Publications, publisher of *Sea Technology;* Miller Freeman Publications, a well-known publisher in the field of forestry, paper, and mining; and Intertec Publishing, which publishes a variety of magazines in the fast-growing fields of telecommunications as well as a variety of other professional and business publications. There are more than 850 magazines and trade newspapers that belong to ABP, and they reach out to approximately 27 million readers across the country in the professions, the sciences, medicine, government, institutional and corporate management. This nation's business press keeps our corporate leaders informed and, as in the recent case of computer magazines, in fact contributes to industry growth. This is business-to-business journalism at its best.

As a publisher of relatively small-circulation magazines, I need the Postal Service. It is the only carrier that can deliver our magazines to our subscribers, and for that reason I would be more than concerned if I thought that the Postal Service's ability to provide universal service at reasonable rates were threatened by technological and other changes. Of course, the Postal Service cannot remain static in the face of these changes, but that does not mean that a massive overhaul of the regulatory framework is appropriate.

The situation that exists today is a far cry from the situation faced by the Postal Service in the 1960s, when ABP was a key advocate of postal reform. At that time, the Postal Service was plagued by work stoppages, deteriorating facilities and skyrocketing costs, and was propped up by hundreds of millions of dollars per year in subsidies. As a result of the Postal Reorganization Act of 1970, politics has effectively been removed from the Postal Service and, through the establishment and operation of the Postal Rate Commission, all mailers are entitled to a fair hearing on postal rates while the Postal Service has been able to meet the congressional policy goals of universal service and reasonable rates.

We understand that the Postal Service wishes to be free from some or even all of the regulatory oversight it now faces, and we have some sympathy for the proposition that even a governmental business enterprise such as the Postal Service must be able to respond to market conditions within a reasonable time frame.

But even this case can be overstated, and has been. Although at the fringes, and almost exclusively for service reasons, there are some daily and weekly publications (in addition to the large daily newspapers) that use small amounts of alternate delivery, we do not, and the vast majority of publications do not. Yet the Postal Service has claimed that it is losing "market share" even in the publications field, a statement which we believe to be simply incorrect and which the recent hearings confirmed. In fact, the Postmaster General has recently gloated over having put Publishers Express, one of its very few competitors, out of business.

Although diversion of periodical mail to alternate hard copy delivery should be a non-issue, and even though diversion of hard copy periodicals to electronic format may one day become a legitimate threat (electronic products are generally supplement, not displaced, hard copy products) we are concerned about the potential economic impact upon the Postal Service of diversion of first-class mail to electronic format. However, this problem cannot be solved or even ameliorated by shortening Postal Rate Commission proceedings or providing additional pricing "flexibility" to the Postal Service.

That is, nothing that this Congress does can or even should stymie the growth of electronic media and communication. Rather, ABP submits that the Postal Service response should be to improve service, cut costs, increase productivity and efficiency and in all respects perform better than it ever has in the past. It must put an end to labor costs that seem to escalate irrespective of flat or even declining mail volumes, and the flexibility it should be seeking is flexibility to manage its workforce and its contracting out procedures in such a way as to minimize the costs of moving the mail.

One area where the Postal Service has placed emphasis, but perhaps not enough, is automation. My publication, *Buildings,* like most of those published by ABP members, is barcoded, which saves the Postal Service and mailers several cents per copy. Unfortunately, even though the Postal Service Governors stated in their March 4, 1996 decision on the Postal Rate Commission's Recommended Decision that "Barcoded mail produced by customers is essential to the success of the Postal Service's automation program, the Postal Service has yet to deploy flat sorting machines that can handle tabloid size publications and newspapers, of which there are billions of mailed copies per year. We understand that the equipment does exist to perform automated sortation of periodicals larger than standard size, and therefore to save the Postal Service the manual sortation costs, but for reasons we do not understand deployment is extremely slow and not expected to get much faster. Here is a way for the Postal Service to improve efficiency, lower costs and lower rates, totally apart from the Postal Rate Commission, and we urge you to urge the Postal Service to get on with it.

Automation and productivity increases may well be essential to the future of the Postal Service. However, weakening or even eliminating the role in postal rate setting now performed by the Postal Rate Commission would, in our opinion, be a big mistake. I know that some argue that the Postal Rate Commission proceedings are too slow and that its role prevents the kind of flexible price response that the Postal Service must be permitted.

As long as the Postal Service is granted a monopoly over most of this nation's mail and tens of billions of dollars of revenues, and as long as only huge mailers receive a sympathetic audience at Postal Service headquarters, it is essential that an independent Postal Rate Commission provide assurances that the policies of the Postal Reorganization Act make their way into rates and provide opportunities for all mailers to participate in the ratesetting process. I testified in the reclassification case, and I know that my views and those of the other more than 100 witnesses were heard and considered by the Postal Rate Commission. I have no confidence that my views would be considered by a Postal Service authorized to set its rates unfettered by regulation.

In addition, as a participant in the most recent proceeding before the Postal Rate Commission, I have come to realize why these proceedings take approximately 8½ months from the date of the filing until the Commission begins consideration of a massive amount of testimony and data, in preparation for the issuance of an opinion only 10 months after the filing is made. While, I suppose, that process could be shortened marginally, there is no way to shorten it substantially while assuring the parties their rights to a full and fair hearing on the record. There might well be a way for Congress to grant the Postal Service limited ability to modify rates or engage in experimental services—although it has certain flexibility today—in those

relatively few areas where there truly is effective competition such as, perhaps, express mail or parcel post, but as long as the Postal Service continues to see phantom competition around every corner, care must be taken that the Postal Service be closely regulated in this regard.

We do not deny that, without any change, challenges lie ahead for the Postal Service, and as I hope I have stressed, my company and publishers everywhere absolutely depend upon the continuation of a strong universal and reasonably priced postal system. Although ABP believes that more harm than good would flow from a loosening of the regulatory process to permit greater rate setting flexibility by the Postal Service, even if the reverse were true, it should be obvious that the fundamental problems of poor service, increasing costs and diversion to electronic media will be largely unaffected by any such changes. Therefore, precipitous change along these lines is likely to do harm and virtually certain to fall far short of solving the problems.

It is for that reason that ABP supports the creation of an independent commission to accomplish what the Kappel Commission accomplished in the late 1960s: To investigate the core problems facing the future of the Postal Service and develop solutions to those problems. To be sure, such a commission would and should study rates and ratemaking flexibility, but it should also study management techniques like contracting out, analyze the Postal Service's automation program, address the highly problematic area of labor-management relations and determine whether or not the Postal Service should expand its product line or contract its operation in the face of electronic diversion.

We stress, however, that neither Congress nor this Commission should function in a crisis mode, because there is no crisis today, as there possibly was in 1970. There are problems, and the solution to those problems can best be developed on the basis of inquiry with broad participation by all concerned. ABP would be pleased to work with the Subcommittee, the Postal Service and all other interested parties to develop the facts on which real solutions can be based.

Thank you for the opportunity to express these views.

Chairman STEVENS. Mr. Cassidy.

TESTIMONY OF LEE M. CASSIDY, EXECUTIVE DIRECTOR, NATIONAL FEDERATION OF NONPROFITS

Mr. CASSIDY. Thank you, Mr. Chairman. I will show my appreciation for the opportunity to be here by using much less than the 10 minutes allotted. My prepared testimony includes a number of comments that I hope you and the Members and staff of the Subcommittee will read and consider. I will make just one point now having to do with the vision our members have for the Postal Service of the future.

When we received your invitation to testify, we surveyed our members so we could honestly represent their current views. Our membership is national, covers more than 300 organizations in virtually every State in the Nation, including your own. So the totality of comments we received from our members is a pretty good indication of the way medium-sized and smaller nonprofit mailers view the Postal Service today and how they would like to see it changed in the future.

I have tried to distill their comments into something coherent, and I think this is it. They would like to see the Postal Service act more business-like. They do not want it to become a business. For them, perhaps the most visible part of acting business-like is that they would like to see the Postal Service operate as though their customers' business were appreciated.

My board chairman works in a tiny town outside of Milwaukee. His charity is the largest employer and by far the largest mailer in town. He complains weekly that his needs and requests are gen-

erally ignored by the postmaster and other postal employees. Another board member is the largest employer and by far the largest mailer in northern Mississippi and probably in the State. He makes the same complaint. A member from St. Paul told me that the only unfriendly clerks she comes across in what she says is a friendly town work in the post office.

This one really rattled me. My 21-person board of directors was unanimous in telling me that no one from the Postal Service has ever called or come by to say thank you for your business. They tell of being treated as though they were necessary evils, not a source of revenue. They tell of a postal bureaucracy that is more concerned with rules than finding ways to help customers solve problems.

Two people I spoke with told me that they have been treated that way for so long that they no longer think of themselves as customers, but as supplicants before a Federal agency. One person said that the only other time she felt the same way was when she went to a bank to borrow money. She said that she had the option of going to another bank, and did, but she can't take her business to another postal service.

So the one point that I want to make, and it is one that is buttressed with numerous specifics in my prepared testimony, is that my members want to feel that their business is appreciated, that the people who take their money understand that jobs are created and maintained because of the business the customers bring to the Postal Service. That is their vision of the Postal Service of the future and their plea for the Postal Service of the present.

They believe that the best way to achieve that is to have continuity in the direction and management of the Postal Service. They want the next Postmaster General to stay on the job for more than a few years. Mr. Runyon has begun a trend, I think, toward more than 3 or 4 years. Whether continuity means a higher salary, hiring a younger person, or all of the above, there is no unanimity among my members, but they do know that each time the top position changes hands, so does the direction of the Postal Service. They see those changes in West Virginia, Mississippi, Boston, Chicago, South Dakota, and Nebraska.

They understand that it takes time to change a bureaucracy and that having a new postal chief executive every few years means that each one spends most of his tenure trying to put his own imprint on the Postal Service and then leaves long before that imprint takes hold. Mr. Runyon understands the problem, and I am certain that that is why he's still in the job. Apparently, he plans to stay for a while longer, but he is also apparently looking at a 5- or 6-year time frame and my members suggest that 10 or 12 is more realistic.

They know how changing senior managers interrupts their own operations and they see how changing postmasters general changes the signals from the Postal Service so that the postal bureaucracy has no choice but to hunker down and live by the rules of the book rather than the rules of good customer relations.

I would like to read verbatim just the last paragraph from my printed testimony. "To summarize, the National Federation of Nonprofits want the Postal Service to become increasingly more busi-

ness-like over the next 5 and/or 10 years. The measurement of business-like is to treat customers as customers. We believe that the best ways to achieve that are to develop legislation that will enable the Postal Service to reduce costs; to create incentives to continuity and better management by senior management, including higher salaries; and to insist through legislation, if necessary, that the Postal Service respond to the legitimate concerns of its customers rather than acting like mindless bureaucrats."

As I said at the outset, Mr. Chairman, my prepared testimony contains a number of specific suggestions that we believe, if implemented, can help the Postal Service get to the point where it will be routine for postal customers to hear the magic words "Thanks for your business."

Thank you, Mr. Chairman, for your attention.

[The prepared statement of Mr. Cassidy follows:]

PREPARED STATEMENT OF LEE M. CASSIDY

Mr. Chairman and Members of the Subcommittee: Thank you for the opportunity to present this testimony. The National Federation of Nonprofits represents more than 300 organizations which raise funds through direct response methods, primarily direct mail. They are mostly medium-sized and smaller organizations, but a few are quite large. The majority are charities.

The members of the Federation, along with all other nonprofit mailers, have experienced major increases in their postage costs in recent years. They have also seen restrictions in eligibility for advertising in third class publications, bore restrictive interpretations of existing regulations, and they hear disturbing voices calling for still more changes in the future. The total dollars represented by nonprofit mail are modest when compared with commercial mail, but the extent of change, and the problems, experienced by nonprofit mailers in recent years have greatly exceeded those of commercial mailers.

So we feel especially qualified to discuss our difficulties with the way the Postal Service operates, and to suggest some actions that might improve the situation.

We believe the Postal Service should continue to become more businesslike in the way it operates. We do not believe it should become a business.

There's no question that the Postal Service is schizophrenic . . . neither a private business nor a government agency in the usual sense. But that's what Congress intended it to be, and we don't see that as necessarily being a problem. We believe that, within the framework of the 1970 legislation, it can continue to be schizophrenic, but also act in a healthy manner.

Congress has considered the public service roles of the Postal Service before, during, and since the 1970 Reform Act, and each time has reaffirmed that those roles should continue.

We have not heard Postmaster General Runyon call, as some others have, for privatization of the Postal Service. He knows, perhaps more than most, what remaining a creature of government entails.

It means that local post offices are a gathering place, and a bulletin board for other government agencies including the IRS, and should continue to be.

It means that mail for the blind and other handicapped people is carried at government expense, and should continue to be.

It means that those organizations designated as tax exempt pay lower postage rates than commercial organizations, and that's the way it should continue to be.

And there are numerous other public service responsibilities that should remain.

But acting more businesslike, with or without public service obligations, means that the Postal Service must control its costs, as every business must. Yet, in spite of the billions of dollars of automation equipment the Postal Service has acquired over the last several years, labor still represents more than 80 percent of total costs, and the number of employees is at an all-time high.

Clearly, that figure must come down if the Postal Service is to become efficient and competitive. It will make no difference how much revenue the Postal Service receives if it can't control its costs.

The Postal Service must be able to negotiate contracts that can result in lower labor costs over time. The current system works to prevent that. So, if the Post-

master General has asked for legislation that would eventually result in lower labor costs, and I hope he has, we're in favor.

Acting more businesslike includes establishing continuity of management. Continuity means two things: Keeping the chief executive in place long enough to have his ideas take hold, and developing potential successors to that position.

Only one Postmaster General has come from the ranks, and that says that the Board of Governors and the previous Postmasters General haven't assured that potential successors are in place. There's a learning curve for every person in every position, and the Postal Service and the American public would be better off if the curve could be navigated before, not during, a tenure as Postmaster General.

More important, though, is assuring that the chief executive stays for 10 to 12 years. It takes that long, in any large business, for the chief to learn the organization and the job, propose changes, and see them through.

That almost certainly means that a new salary structure needs to be developed for the top rung of postal executives. While many of today's corporate CEO salaries are out of line with reality, the Postmaster General is running a large organization that everyone wants to be more like a business, and therefore ought to be paid more like a business executive. $500 to $800 thousand doesn't seem to be out of line, and would be one factor in keeping a good Postmaster General for more than a handful of years. Other senior positions should carry comparable salaries.

Perhaps the most important aspect of acting like a business is to recognize that the people who pay postage are customers. Customers are the lifeblood of any business. They are where all the revenue comes from. But no one among the Federation's board of directors, has ever been called or visited by a Postal Service employee to be thanked for his or her business!

My directors complained that they are made to feel like supplicants before a large federal bureaucracy, rather than customers. One member, not a member of the board of directors, said that the only clerks in her city of St. Paul who are unfriendly are those in the Post Office.

Acting like a business also means that sometimes the customer is treated as though s/he is right, even if s/he isn't. Again in St. Paul, a postal inspector has insisted that a small church pay back postage for their newsletter, because it turns out that the church committed a technical violation of the Domestic Mail Manual. The amount of money is very small, for the Postal Service: $1,600. For the church, it represents a large amount.

But is it the best use of resources for a postal inspector, whose main role presumably is to detect and prosecute fraud, to worry about a $1,600 shortfall over a two-year period? And is it the best way to train Postal Service employees in how to treat customers like customers when the Postal Service insists on recouping a few dollars from a church that made a technical error, which went unnoticed by the Postal Service for two years?

Can you imagine Federal Express taking such an action? In fact, can you imagine any business taking such an action?

Another situation, currently at issue, is also instructive. As part of mail classification reform, the Postal Service has issued regulations which insist that, to qualify for most automation discounts, bulk mail must be placed in trays with a minimum of 150 pieces in a tray. The entire mailing industry is opposed to that regulation, because 150 bulky letter envelopes cannot fit into a tray. A simple solution has been suggested: a minimum of 150 pieces or a full tray. The entire mailing industry supports that minor change, but the Postal Service refuses to accept it.

Can you imagine any other business that would refuse to accept such a sensible suggestion from its customers?

To summarize: the National Federation of Nonprofits wants the Postal Service to become increasingly more businesslike over the next 5 and/or 10 years. The measurement of businesslike is to treat customers like customers. We believe the best ways to achieve that are to develop legislation that will enable the Postal Service to reduce labor costs; to create incentives to continuity of senior management including higher salaries; and to insist, through legislation if necessary, that the Postal Service respond to the legitimate concerns of its customers, rather than act like mindless bureaucrats.

Thank you for your time and attention.

Chairman STEVENS. Well, thank you very much. I think you gentlemen sort of highlight the dichotomy that faces us. I am not sure that many people can get as vivid a recognition of the interest of

Congress in the subject before us as you can by looking at this table.

You are asking us to create a commission to bring back to Congress information on which it should act in a bipartisan way and put aside special interests and put aside all provincial aspects of our activities here. I am constrained to tell you that I am not sure a commission would bring any more people back to this table. I will give that some consideration and talk to other members, but many people accuse us today of just pushing off our responsibility by creating another commission.

I think our friends from the labor movement will probably have some point of view on that because, Mr. Estes, the one thing you would like to see changed is some of the labor costs, I take it—you and Mr. Wendler. That commission is not going to have any greater ability to do that than anyone else. I will talk to the other Members of the Committee about it and see if that is what they would like to do.

I think you should be aware that we probably are facing legislation once we get to the floor that would totally privatize the Postal Service. Any piece of legislation we take out there today, I think, will face an amendment that would demand that the Postal Service be totally privatized, and so I would urge you to consider the consequences of not making any decisions now toward some reform and pushing it off until another Congress through the commission process because, as you say, the commission could not report back soon enough to get any action by this Congress.

All of you have testified that you don't think the Postal Service should react to competition. Do you not see competition out there for the Postal Service now? The witnesses that have come before us here have delineated a whole sizable area of competition which has taken away revenues from the Postal Service already. Are you in disagreement with that testimony?

Mr. ESTES. No. Clearly, there is competition in the ability to deliver messages and there probably always will be alternates to that, but I think the question ought to be not whether there is competition. The question should be is the system that is in place now managed the best as it can be and can there be things brought to that system which would assist in its management? Competition itself can be healthy if it results in better management, better cost control, better innovations in accomplishing the mission.

So what bothers us, Mr. Chairman, is that we are not suggesting that anything be pushed off and we are not suggesting that Congress for a minute abrogate the responsibilities which it has, but we are urging that we make every effort to bring to you not a dichotomy of views, not a whole litany of special-interest representations, but an effort to coalesce what can be the best and then let Congress decide, in the public interest, if that is the way the country should go.

In this process, we would be developing, we think, among the mailing community a consensus which is important. As you know, in our system of government what people support and encourage and are excited about is important for the direction that we would suggest going. The post office touches us all. You know that, we know that, and we just think it is exceptionally important that we

not tinker with it, but that we look at it very, very carefully, as you must and will do, but when you do that, we bring to you the best we can

Chairman STEVENS. Mr. Wendler?

Mr. WENDLER. As a publisher of a second-class periodical, I know who my competitors are and we call on advertising prospects and my competitors are right there. The reason why I am so concerned about this as a second-class mailer is that I have nobody calling on me as someone who might be able to deliver this magazine. I feel that I have no choice, really, at all but to use the Postal Service, and consequently I feel very strongly and am very fearful about being a small publisher from Cedar Rapids, Iowa, that if the powers of the Postal Rate Commission are taken away, I will lose my opportunity to speak out.

Chairman STEVENS. Well, I think you should be fearful. I have had Members of Congress talk to me and say the whole thing should be privatized, that there is no reason for different classes of mail as they exist right now, that private business would not have classified mail in that way, that it is a holdover from the old Post Office Department and that we are subsidizing a whole series of businesses because of the cross-subsidization from first-class mail that pays for the basic underpinning of the Postal Service.

Mr. Wendler, you represent a substantial portion of the Postal Service. Why should I burn the midnight oil and draft a bill here to get it out so we might pass it this year to partially reform the Postal Service to meet some of these objections if you all don't want that? You will be able to stop the bill as well as the other people can stop it.

I really think you ought to reconsider your proposition to us because there are a few people in the House still and a few people over here still that would preserve some portions of the postal system. I think the vast majority of Congress today would privatize it. I think whatever bill we take out there may well face a privatization amendment and it may win.

With due respect, Mr. Estes, you are asking me to put it off. You are asking me to create a mechanism that could not lead to a result this year to meet the demands of the competition that the postal system has outlined to us.

Mr. Cassidy?

Mr. CASSIDY. Mr. Chairman, the Postal Service ought to be responding to its competition and I am not sure that it understands what the competition is.

Chairman STEVENS. They cannot. They have delineated at least six different things here where they were—two here in the record, four that we know about, where they lost substantial volume because of competition. They were unable to meet the offer of a competitor to their customers, mass customers. Under the circumstances, they were not able to go through the Postal Rate Commission in less than 10 months, so they lost that business.

Now, I understand what you are saying about the stability of first-class and the stability of other classes of the mail, but there is competition out there that is taking away from the Postal Service some of the revenues necessary for modernization.

Mr. CASSIDY. The Postmaster General himself has recently talked about how WalMart has insisted that its vendors deal with it through electronic means, bill electronically, or bill them electronically; that Citibank is encouraging its customers to do business via computer. Yet, a year ago when the Postal Service said that it planned to offer a special rate for courtesy reply envelopes, it took no action upon the—or took a negative action upon the Postal Rate Commission's recent suggestion that a shell classification be created. Every day that there is not such a shell classification, more people will begin to pay their bills electronically, and that is business that the Postal Service is losing, I believe, by its own inaction.

Chairman STEVENS. Well, I think it is losing business all right because I think it is not enforcing the monopoly statute because I don't think it can win. I think they realize they would not win that suit either. So, as a practical matter, the system needs to be modernized if we are to deal with that.

It is just an aside, but 12 years ago I suggested that we go to electronic mail and the Congress turned it down. It does seem to me that they would turn it down now, too. I don't think Members of Congress seek to expand the jurisdiction of the Postal Service. That is my reading. Maybe yours would be different, but that is my reading of Congress today.

Let me put it to you this way as a question. Do you think the Postal Service can survive well into the next century without some change in their basic statutes today?

Mr. ESTES. I think the most important purpose that the Postal Service serves today is the first-class, third-class universal mail at universal rate concept. I think, Mr. Chairman, that has to be preserved and we have to fight hook, tooth and nail to make certain that that is preserved in all parts of the country for all mailers of a certain class. I really don't think that if the system were privatized lock, stock and barrel we would see that happen. I think a Postal Service, regenerated, reorganized, focused, possibly limited in certain areas that it would function, controlling its costs, operated managerially properly—yes, I think it can survive for a long time.

Second, I think one of the confusions and one of the difficulties is the lack of some consensus, some understanding or unanimity on what should the mission be. Should the Postal Service compete in all areas? Maybe it shouldn't. Maybe we should step back and say, look, you can do some things very well and some things the private sector can and should do better. That is the sort of deep, head-scratching analysis that we would like to perform and do and bring to you for your consideration. That is what is behind this.

Yes, it is going to take a little time; yes, there will be some criticism; and, yes, we are going to have to hold off intemperate action like privatization, which would be, in our judgment, a total disaster.

Mr. CASSIDY. Let me repeat a phrase that Mr. Estes used, "controlling its costs." Those of us who are current customers of the Postal Service want to see two things—costs go down—that is critically important—and we want to see revenue go up because to the extent that more people are using the Postal Service more and to

the extent that the Postal Service can drive costs down, our rates will become more or less stable.

So those of us who are already customers have an absolute, major stake in seeing increased business for the Postal Service. As I just pointed out, there is at least one example, and I am sure that there are others, where the Postal Service isn't reacting quickly enough to proceed in the face of real competition.

Chairman STEVENS. Well, for the services that it performs where it doesn't have a monopoly, what is the justification for us to say as a Congress that the Postal Service, which is now a semi-government entity, must go through another creature created by the Congress and the government in order to set rates? For the non-monopoly services, why should the Postal Service be regulated at all through the Postal Rate Commission?

Mr. ESTES. If engagement in those activities, Mr. Chairman, results in the monopoly-protected area of the activity financing that engagement and if, then, what we have, in a sense, is truly unfair competition with respect to the private sector and a monopolized, financed sector of the government competing with that private sector, that, in our judgment, is not part of our system. That is not the way we think things should be operated.

Now, we could say, well, let's set up a strict accounting mechanism so that institutional and attributable costs will never seep in and there won't be this mission creep so that the function of the post office as a monopoly can be used in an unfair way to compete with good-faith private efforts that are doing a good job, that are providing a service.

Could I make just one other quick point? We have 40 days left, roughly, I guess—you would know better than I—legislative working days. We are just terribly concerned that moving ahead under those conditions—even though the post office is huge and it is complex, in many respects, because of its omnipresence throughout the society, it is very delicate and we have to just be extremely careful where we adjust it and where we don't, and that is why we are strenuously and earnestly urging you to consider this larger-picture approach. I made that point. I won't make it anymore.

Chairman STEVENS. Well, are you familiar with the testimony we had from the representatives of the postal systems in four different countries as to what has happened in those countries with regard to modernization?

Mr. ESTES. Yes. I can't say I am as familiar as you are, Mr. Chairman, but I have looked at it and considered it, and the question, of course, comes frequently for us in this country can we learn from other countries, and the answer is obviously, yes, we can, but in that learning process we have to filter what those other countries are doing through an American filter.

I am constantly amazed by my friends that come over here from Western Europe for the first time, as I am sure you are, how gigantic and huge our country is, let alone Alaska, but the whole country, and the diversity in culture and the diversity in interest and makeup that we have. People from New Zealand, not necessarily Australia, and from Western Europe, particularly, are fascinated by that. To take a government system out of essentially social

democratic societies—because it is working well there, yes, we may learn something. Should it be a model for us? Probably not.

Chairman STEVENS. No, I don't say it would be a model, but it certainly ought to be a warning and it ought to be a warning to your industry because I don't see second-class mail surviving in a privately-operated postal service, not on the basis that it is today with first-class paying the bulk of the costs and second-class and other classes taking up from there. That is not going to be the result, and they demonstrate that that is not the case in those other countries. Rates are going up in the non-first-class area in those countries.

Mr. WENDLER. As a Washington outsider—somebody from Cedar Rapids, Iowa, coming here—I am very pleased to hear such concern about the balancing of costs and revenues, but there are public policy considerations which I think are important as part of this and which make the Postal Service a service and not necessarily a business.

Chairman STEVENS. You sound like you are from Alaska, Mr. Wendler.

Mr. WENDLER. Thank you.

The public policy is widespread dissemination of information, which I think works very well. With the way second-class is organized right now, I can send a magazine to Grand Rapids, Michigan, to Manhattan, to Chicago, to Fairbanks, and it is equal across the board and that is a public policy consideration that I would hate to see get lost if we are just going to look at costs and revenues.

Chairman STEVENS. Well, that is true, but I face arguments from my friends in the Postal Service all the time about the cost of delivering parcel post in Alaska. It is a uniform cost across Alaska and they would like to put zones there, which would make it totally unaffordable. So I think when you look at it, there are a lot of policy decisions that have to be made and I think my task as an Alaska Senator is trying to see to it that we preserve the concept of a Federal connection to the Postal Service. I don't see that existing much longer unless we can get some modernization and stop this loss of revenue that is taking place.

I appreciate you gentlemen coming. I want you to know that I did read some of the statements on the plane coming back yesterday. I still think we ought to go ahead and try to draft up a bill to meet part of the Postal Service's problems, but we will draft a bill for a commission, also, and see what the Committee wants to do. If they want to put it off until the next watch, this is the end of my watch this year. I will not be Chairman of this Committee next year.

Mr. ESTES. We hope you will still be involved in one way or another.

Chairman STEVENS. Well, with the new rules, I may not be.

Mr. ESTES. I understand.

Chairman STEVENS. It may be my last year on this Committee. We will wait and see.

Thank you very much, gentlemen.

Mr. CASSIDY. Thank you, Mr. Chairman.

Mr. WENDLER. Thank you.

Chairman STEVENS. Now, we have another group, the second panel. Well, let's proceed now. Mr. Brinkmann, you are the president for Postal and Regulatory Affairs in the Newspaper Association of America. Why don't we start with you first? We started from the end last time.

TESTIMONY OF ROBERT J. BRINKMANN, VICE PRESIDENT, POSTAL AND REGULATORY AFFAIRS, NEWSPAPER ASSOCIATION OF AMERICA

Mr. BRINKMANN. Thank you very much. I appreciate the opportunity to be here this morning. I have taken the liberty of not preparing a written statement, since we submitted one with Mr. Sturm's testimony several days ago, but I appreciate very much the opportunity to come before you and appear on this panel with my colleagues.

Mr. Chairman, we appreciate the interest of this Committee in postal matters and the look that you are taking at postal reform now. I think several things need to be kept in mind as this Committee considers the various proposals before it.

First, is the fact that the Postal Service is a very, very complex institution, and one should take the idea of change very, very seriously. If one makes a mistake and passes something that is not a good idea, the ramifications and repercussions of that mistake will exist for a long time.

Second, I think you may well find that there really is a consensus that the system isn't broke, and the question is: Do we really need to fix it? Now, I am sure different individuals and different groups will vary as to how much they agree or disagree with that statement, but I think a general consensus is developing that radical change is not something that is really good for the institution at this time.

Quite frankly, as we view the various proposals that have come before the Committee, we see some that we feel do constitute radical change; one, as you have mentioned, is the concept of privatization.

Another one, however, is changing the pricing mechanism. And I would suggest to you that a change in the pricing mechanism really is a radical change because it goes to the fundamental nature of the postal system. It fundamentally and inalterably changes the service incentives of the institution and who bears the overhead costs of the institution. It changes that dynamic in a way that would make it very difficult to undo.

Finally, it doesn't really do anything to change the cost structure of the institution. I think if you look over the testimony of the nine different groups that you have had in the last day-and-a-half, you will see a common theme: That if there is a problem, it appears to be the costs. If the costs are the problem, changing the price mechanism really doesn't go to the underlying nature of the costs.

Any business, if it wants to lower its prices for its customers, has two choices. One, it can lower its profit margin or, two, it can cut costs. If a private company lowers its profit margin without cutting costs, it feels the ramification of that action in the stock market with the effect on dividends and shareholders. The Postal Service

doesn't have stockholders nor shareholders, and that option really isn't available to it.

Chairman STEVENS. Can it also increase revenue?

Mr. BRINKMANN. It can increase revenue.

Chairman STEVENS. Aren't there three options?

Mr. BRINKMANN. Well, I think the third option, increased revenue, is really the flip side of lowering costs. I mean, if you lower costs, you basically increase your revenue.

Chairman STEVENS. Well, I don't see that as being exclusive, and I think that is what the Postal Service talked to us about—mechanisms increase revenue through competition, particularly in the non-monopoly area. What do you say about that?

Mr. BRINKMANN. Eighty percent of the revenue of the Postal Service comes from the monopoly area today.

Chairman STEVENS. Right.

Mr. BRINKMANN. In one of those areas, I think it gets back to costs. We have heard the Postmaster General mention that the Postal Service lost a fairly large contract recently with a large department store because it couldn't come in and negotiate parcel rates.

Chairman STEVENS. Right.

Mr. BRINKMANN. If one accepts the premise that rates really have to cover costs and one looks at the parcel rates today, I think there is probably a general consensus that the parcel rates of the Postal Service today barely cover its costs. Indeed, many would allege, I think, that they don't cover their costs.

If that is the case—yet the Postmaster General complains that he doesn't have the flexibility to negotiate a lower rate and have the rates cover costs—there is really not any room to negotiate a lower rate unless you are going to break the principle that rates have to cover costs, and allow the Postal Service to negotiate a rate with this large department store that doesn't really cover its costs.

So it seems to me at least in the parcel business, it comes back to the message that to the degree there is a problem, the problem really is costs, and I have seen very few of the proposals before you that really tend to focus in on that.

Chairman STEVENS. Mr. Sackler?

TESTIMONY OF ARTHUR B. SACKLER, VICE PRESIDENT FOR LAW AND PUBLIC POLICY, TIME WARNER, INC.

Mr. SACKLER. Thank you, Mr. Chairman. Time Warner is pleased to have the opportunity to participate in this interactive discussion of postal reform issues and we commend your interest and that of the Subcommittee in addressing what is a very fundamental matter for the Nation. Now, we did submit a statement and I will attempt to very briefly summarize it for you.

In addition to being one of the largest users of the mails, Time Warner is both a content and a service provider for the Internet, one of those competitive areas that I think you have been told about. We operate one of the most popular sites on the World Wide Web called Pathfinder, which is experiencing an average of 27 million hits or communication contacts a week. We also are providing Internet access through one of our cable television subsidiaries and

have a full-motion video, completely interactive service in place in Florida.

All of us who depend upon and care about the postal system have a choice. We can either embrace the future or resist it. As you know very well, there is a communications revolution underway which the Congress recognized in accomplishing the most fundamental overhaul of the Communications Act in more than 60 years.

If you look at the alliances, start-ups, mergers, and more that that has stimulated in telephone, cable, wireless and, of course, the Internet, you can see that this change has done a lot to precipitate more competition to the system. So how can we permit the still essential service of hard-copy delivery be left in a situation where its ability to compete is hobbled?

We think the time for postal reform is right. Although, thanks to the great efforts of its management and its craft workers and the rest of the employees, the Postal Service appears to be functioning exceedingly well, our focus cannot just be on the here and now. Rather, our focus has to be broad enough to encompass the competition and contemplate the future of the system in relative terms. Mail has to be looked at as a part of the overall communications universe.

The Postmaster General, as you have mentioned, has cited five of six of its product lines where it is losing business. He has cited examples of divergence from a number of big customers which were discussed in the last panel. Time Warner has been able to see firsthand the direction of communications away from hard copy. Pathfinder, for example, did not exist even 2 years ago. The nearly 30 million hits it gets a week would not have taken place. Many of those communications are to obtain information from our magazines or our books and would have been, we believe, through the mail.

E-Mail has grown tremendously. I would respectfully suggest, Mr. Chairman, that the Subcommittee invite to testify at a convenient time responsible members of the electronic community who are working on valid cyber signatures, cyber cash and other systems that will make business transactions routine, reliable and secure by electronic means, creating vast, new competitive potential to the Postal Service.

The warning signs of market share slippage and growth in competing media tell us, anyway, that the Postal Service must have some more flexibility to tailor its businesses and respond to competition. You have asked for our vision of the future for USPS. We want it to, and believe it can be a thriving one for every user and the general public with some less than sweeping changes.

As we and others have begun to lay out in these hearings for you, the new and dramatically growing electronic communications medium does pose a major competitive threat to significant parts of the Postal Service's business for the next 5 to 10 years. Just today, the *Wall Street Journal* reported on Microsoft's plan to expand into electronic banking, where there already are more than 9 million users.

But as with most business threats, there is also an opportunity for those who can discern it. Certainly, in the Postal Service's case,

many of the electronic orders predicted for the Internet will result in something tangible to be delivered. If USPS can nimbly shift to capitalize on its unparalleled asset, its delivery system, to capture new markets by creating new products in that area, then it may be able to offset volume and revenue lost elsewhere.

USPS managers must spot market changes and devise responding products rapidly. It is our responsibility to support at least limited change by the Congress to permit those managers to do their jobs in the way they should. As you requested, we have three suggestions that we believe might better position USPS for the future.

First, price caps. They have worked well in other domestic environments, as well as for a number of foreign postal administrations. The caps would have to be set below inflation as measured against the standard we believe would be appropriate, the employment cost index, and apply across the board, subject to necessary rounding. Permitting USPS to raise rates no more than annually to some pre-set limit would provide both a reward and an incentive to the Postal Service. It could have a very abbreviated proceeding before the Commission for the purpose of verifying its numbers only. It would be an easy and fast change in pricing and offer the flexibility to respond with alacrity to the competition.

At the same time, this avoidance of a full-scale proceeding would serve as an incentive to stimulate USPS to keep its cost increases within the limited zone of permissibility. Price caps must constitute a ceiling for price increases. Rather than any guaranteed annual price increase, we suggest an incentive compensation plan be developed, much as is the case in foreign postal administrations that have corporatized, which is directly linked to the Postal Service's success at limiting rate increases by being more productive and not reducing service. We want to restrain the growth of fat and not cut into muscle.

Second, the governors should be able to modify a rate recommendation by a super-majority vote. We would also permit modification upon first receipt of the case and not have it go up and down and then back for modification. These changes would leave more to the judgment of the presidential appointees responsible for its operations what is in the best pricing interest of USPS in light of competition and other factors. Finally, the governors should be able to modify in more cases than just those where the Commission has failed to recommend revenue sufficient to break even, such as, for example, operations or policy reasons.

Our third suggestion is to experiment with contracts. Time Warner has been one of those parties which has advocated enabling the Postal Service to contract. Many other interests oppose granting this authority in the belief that contracts would only benefit larger mailers at the expense of smaller ones and that these larger companies would be able to out-bargain the Postal Service. Our experience in reaching contracts in other countries has taught us graphically that that will not happen.

These contracts typically work in two directions, Mr. Chairman, with rate and volume guarantees. If a mailer falls short of a contracted volume, as we have occasionally and ruefully experienced, it is still responsible for paying as if it had that volume. This helps every other mailer when there is an economic downturn or just

misfortune in the individual business. Contracts can also create the potential for the pioneering of work-sharing opportunities, as we have discovered in Canada.

So we would urge the Congress to authorize an experiment with contracts. This would be for a very limited number of contracts and for a limited period of time only. The Postal Service and the mailer would be free to reach whatever agreement makes mutual sense, provided the contract would be self-sustaining and not create or rely upon cross-subsidization over its life. The contracts should be distributed among mailers of a variety of sizes. The Postal Service and GAO would then be required to report on and evaluate the contracts.

I will close with a note on those foreign administrations who came and appeared before you, Mr. Chairman, as well as some of the others. Are they a perfect model for the United States? Of course not. By the same token, they should not be dismissed simply because of social, size, or geographic differences. As much as they have to learn from us, we have to learn from them.

Again, Time Warner believes that the time is ripe to consider certain reforms of the postal system. We commend you and the Subcommittee and urge you to pursue the matter. That concludes my testimony and I certainly look forward to the interactive discussion.

Chairman STEVENS. Thank you.

[The prepared statement of Mr. Sackler follows:]

PREPARED STATEMENT OF ARTHUR B. SACKLER ON BEHALF OF TIME WARNER, INC.

Good morning Mr. Chairman. Time Warner is pleased to have the opportunity to provide its views to you on the important question of postal reform. We are particularly intrigued by the format of this panel, and very much look forward to the "interactive discussion" of issues presented over the past two days. My name is Arthur B. Sackler and I am Vice President for Law and Public Policy of Time Warner Inc. I am also the Executive Director of the Mailers Council, an umbrella coalition of virtually every mailing interest. My appearance today and any positions that I take, however, should not in any way be attributed to the Council. They represent the points of view of Time Warner Inc., only.

Time Warner is one of the world's leading media and entertainment companies, with interests in magazine and book publishing, recorded music and music publishing, filmed entertainment, broadcasting, theme parks, cable television and cable television programming. Time Warner is one of the largest users of the mails for our magazines, books, audio and video products, promotions, billings, and more.

Time Warner also is both a content and a service provider for the Internet. We operate one of the most popular sites on the World Wide Web, Pathfinder, which is experiencing an average of 27 million "hits," or communications contacts, a week. We also are providing Internet access through our cable television company in Elmira, New York, a venture known as Linerunner. And, finally, we have a completely interactive, switched digital video, voice and data "Full Service Network" in place in Orlando, Florida, currently serving approximately 4,000 customers.

Why Postal Reform Should Proceed Now

Mr. Chairman, all of us who depend upon and care about the U.S. postal stem have a choice: we can either embrace the future or resist it. Whether or not some in the postal arena wish to acknowledge it, there is a communications revolution underway. This Congress recognized that fact in accomplishing the most fundamental overhaul of the Communications Act in more than 60 years. The changes in business and the provision of communications services that that will stimulate will move with escalating speed. Just look at the alliances, new startups, mergers, and more taking place in telephone, cable, wireless and, of course, the Internet. How can the still essential service of hard copy delivery be left in a situation where its ability to compete is hobbled?

The time for postal reform is ripe.

In one sense, of course, that may lead to some head scratching, frankly. After all, the Postal Service appears to be functioning exceedingly well. It made a record profit last year. Service is at record levels. It appears well on its way to making another sizeable profit this year. The Postmaster General is talking about keeping rates stable, perhaps to the year 2000. That would mean only one general rate increase in nine years, a truly astonishing feat. In short, to all appearances, we'd be risking fixing what ain't broke, and flying in the face of conventional wisdom.

But conventional wisdom is not always either correct or sprung from a broad enough focus. The focus has to be broad enough to encompass the competition and to contemplate the future of the system in relative terms, and not just absolute terms. Even though postal revenues and volume have been generally growing (although so far this year volume is down nearly three-quarters of a billion pieces), mail must be looked at as part of the overall communications universe. The Postmaster General says the Postal Service is losing market share in five of its six product lines. He cites examples with WalMart, Citibank and JCPenney to demonstrate that many businesses, including very large postal customers, are redirecting many of their communications out of the system.

As a large player in telemarketing, cable television and, now, the Internet, Time Warner has been able to see first hand the direction of communications away from hard copy. Pathfinder, for example, did not exist even two years ago. The nearly 30 million "hits" it gets a week would not have taken place. Many of those communications to obtain information from our magazines or our books would have been through the mail looking to subscribe to or buy a particular product.

E-Mail has grown tremendously in popularity, and it is not just confined to supplanting telephone conversations or faxes. It is convenient for displacing hard copy communications. I would respectfully suggest to this Subcommittee that it invite to testily responsible members of the electronic community who are working on valid cyber signatures, cyber cash, and other systems that will make business transactions routine, reliable and secure by electronic means. And this does not just extend to business to business. Count the homes where there are Internet connections, and private citizens who file tax returns or pay bills or bank electronically. It's just the tip of the iceberg. As these systems become easier to use and more familiar, their already significant level of usage will inevitably increase.

The reason, therefore, to undertake postal reform now is looking to the future. The warning signs of market share slippage and growth in competing media tell us, anyway, that the Postal Service must have some more flexibility to tailor its businesses and respond to competition.

The Postal Service of the Future

You have asked for our vision of the future for USPS. We want it to and believe it can be a thriving one. For every overused comparison about the demise of the dinosaur, horse and buggy or Western Union (or even the ill-advised ECOM), there is one about a resurgent cinema or radio, retooled to do successful business battle. The only (also overused) comparison we really need to be concerned about is the ostrich. If our head is not in the sand, we can help USPS reach out to the future. In our view, with some less than sweeping changes, USPS will not only remain viable, it will prosper well into the next century.

To be a bit more specific, as we and others have begun to lay out in these hearings for you, the new and dramatically growing (56 million users now, 200 million by 1999, according to IDC, cited in the March 14 *Financial Times*) electronic communications medium does pose a major competitive threat to significant parts of USPS' business over the next 5–10 years. But as with most business threats, there is also an opportunity for those who can discern it. Certainly, in the Postal Service's case, many of the electronic orders being predicted will result in something tangible to be delivered. If USPS can nimbly shift to capitalize on its unparalleled asset—its delivery system—to capture new markets by creating new products in the delivery area, then it may be able to offset volume and revenue loss elsewhere.

Other opportunities? Well, I'm sorry, but my crystal ball appears to have been misplaced. It will be for USPS' managers to spot and understand the market changes as they happen and devise responding products rapidly enough to take advantage of the opportunities. And it is our responsibility to support limited change by the Congress to permit those managers to do their jobs in the way they should.

So, as you requested, we have three suggestions that we believe, if taken this year, would start us down the road to meaningful reform that will better position USPS for the future.

Suggestions For Reform

Ratesetting. First, we believe that the current ratesetting process is too lengthy and cumbersome to give the Postal Service any hope of responding to competitive pricing changes. We also believe that it contains no incentives to the postal system to constrain its costs. Not every postal management has been as conscious as this one has been of holding down the growth in costs. The process should help guide any set of postal managers in this respect.

We believe, then, that this Subcommittee should take a close look at the concept of price caps. They have worked well in other domestic environments such as the tariffing of telephone rates, as well as for a number of foreign postal administrations, such as in the Netherlands. One important caveat is that the caps would have to be set below inflation as measured against some relevant standard. The Consumer Price Index, as has been widely discussed, may overstate inflation. We would prefer the Employment Cost Index (ECI) as a more realistic measure. The price caps would have to apply across the board because of the difficulty in making price changes differentiated by class and subclass in the absence of a comprehensive and conventional proceeding.

Permitting USPS to raise rates on no more than an annual basis to some preset limit that helps constrain USPS' costs, as below inflation price caps would, would benefit the Postal Service and its customers in two interrelated ways, providing both a reward and an incentive. First, the reward: USPS could have a very abbreviated proceeding before the Postal Rate Commission for the purpose of verifying its numbers, only. It would be an easy and fast change in pricing that does not involve the onerous resource burdens of a general rate case. This would give the Service the flexibility to respond with alacrity to the competition. At the same time, this avoidance of a full-scale proceeding would serve as an incentive to stimulate USPS to keep its cost increases within the limited zone of permissibility. Failure to so restrain its costs, or a request for any reason beyond the established caps would require the Service to go through a conventional general rate case.

But it should be borne in mind that any price caps must constitute a ceiling for price increases rather than any guaranteed annual price increase. To accomplish this, we suggest that an incentive compensation plan be developed which is directly linked to the Postal Service's success at limiting rate increases, by being more productive and efficient, and not merely reducing service levels. In other words, we want to restrain the growth of fat and not cut into muscle.

Governors' modifications of Commission recommendations. The second change Time Warner would recommend would be to adjust the Governors' ability to modify a rate recommendation from the Commission. We believe that a supermajority vote should be sufficient for a modification, as contrasted with the unanimity required by the existing statute. We would also permit modification upon first receipt of the case. We would no longer require that the case be remanded at least once before the Governors could revise a Commission recommendation. This change, too, would confer a great deal of additional rate flexibility on the Postal Service. It would leave more to the judgment of the presidential appointees responsible for its operations what is in the best pricing interest of USPS, in light of competition and other factors.

Finally, we suggest that a necessary condition for giving meaning to the above changes would be that the Governors be able to modify in more cases than just those where the Commission has failed to recommend revenues sufficient to break even (39 USC Sec. 3625(d)(2)). Even with adequate revenues, the Governors may have changes they wish to pursue for operations or policy reasons. Broadening this subsection would grant them that flexibility.

Contract experiments. A third suggestion that we would make is in the nature of a limited experiment. For many years, Time Warner has been one of those parties which has advocated enabling the Postal Service to create rate and service contracts with its customers. We are far from the only customer who would want the Postal Service to have this ability. However, many other interests oppose granting the Service the authority to contract. They apparently believe that contracts would only benefit larger mailers at the expense of smaller ones and/or the general public. They apparently further believe that these larger companies would be able to outbargain the Service and develop contracts with very unequal terms that clearly favor the mailer.

We simply don't believe that would happen. In fact, our experience in reaching contracts in several other countries has taught us graphically that will not happen. These contracts typically work in two directions. They have rate guarantees, but they also have volume guarantees. If a mailer falls short of a contracted volume, as we have occasionally and ruefully experienced, it is still responsible for paying as if it had that volume. This helps every other mailer in the case of an economic

downturn, or just misfortune in the individual business. In the absence of a contract, of course, the mailer simply pays for whatever use it actually makes of the system. No one else benefits.

Contracts also create the potential for the pioneering of worksharing opportunities which benefit all mailers in the long term. A clear example of this took place in Canada, where our publishing subsidiary, Time Inc., utilized our carrier route expertise to help Canada Post develop its own carrier route sorting system which is now employed by its entire customer base.

Therefore, we would propose a test of everyone's speculation and beliefs. We would urge the Congress to authorize an experiment with contracts. This would be for a very limited number of contracts, and for a limited period of time only. The Service and the mailer would be utterly free to reach whatever agreement makes mutual sense, without being restrained by other rate or classification criteria. The contracts would have to be self-sustaining, and not create or rely upon cross-subsidization over the life of the contract. Finally, these contracts should be distributed among mailers of a variety of sizes.

The Postal Service would be required to report at the end of the contractual period. And the General Accounting Office would be asked to do an independent evaluation. Without much risk on revenues, the Postal Service could obtain at least a small sample of how everyone from the smallest businesses to the very largest would respond in a contractual situation, and how the Postal Service itself would do in proposed negotiations.

Foreign Postal Administrations. I would also like to touch briefly on the foreign experience in reforming postal systems. Are foreign postal administrations a perfect model for the U.S.? Of course not. By the same token, they should not be dismissed simply because of social, size or geographic differences. There are lessons to be learned there, even as they strive to learn from us.

The joint hearing held in January certainly presented witnesses who offered much food for thought. It is quite apparent that postal reform is not just a concept in many other countries. As you know, other nations have "corporatized" their postal services. Time Inc. has visited and studied a number of foreign administrations. Our view of what they have accomplished echoes what you have heard. Nonetheless, we have distilled this information into a few key points for your convenience and consideration:

- Foreign postal services have the ability to manage effectively their workforce size through attrition, job training, and new product development. In addition, there generally is an incentive for both management and labor to reduce costs.
- There is a financial reward for performance. This is not a guaranteed salary increase, but is tied to the achievement of specific goals.
- Rate increases are capped and the foreign postal services have substantial freedom to establish rates below those caps. In all cases, rates have either been reduced or at a minimum, increased less than the local CPI.
- Universal service has been an absolute requirement. In fact, many foreign postal services view universal service as a competitive advantage rather than a burden.

Once again, Time Warner believes that the time is ripe to consider certain reforms of the postal system. We commend the Subcommittee and urge you to pursue the matter. That concludes my testimony, and I look forward to our interactive discussion.

Thank you.

Chairman STEVENS. Mr. Cerasale.

TESTIMONY OF JERRY CERASALE, SENIOR VICE PRESIDENT, GOVERNMENT AFFAIRS, DIRECT MARKETING ASSOCIATION, INC.

Mr. CERASALE. Thank you, Mr. Chairman. It is indeed an honor to be invited to participate on the closing panel of this stage of your hearings. You have already heard the testimony of DMA's president, Jonah Gitlitz, and I support that fully and I will try not to repeat any of his statements.

The Postal Service is important to our industry. All mailers need a hard-copy delivery system that provides universal service, reliable service, at a reasonable price. The testimony I think we have heard Thursday and heard today is that it appears the Postal Service is not charging reasonable prices because it can't seem to control its costs. Every mailer wants cost inflation to at least slow and, of course, an absolute decline in costs would be magnificent.

How to achieve that goal is where mailers and the witnesses you heard today and the witnesses you heard on Thursday differ. Some believe the Postal Service should be given flexibility in pricing so that it can be more business-like. Competitors are worried that flexibility means unfair competition. Monopoly classes will cross-subsidize competitive postal classes. Some users, many first-class users, are concerned that the Postal Service will favor bulk business mailers at their expense with price flexibility.

So what do we do? There are really three stages we can take. We can have very limited changes to the legislation, the Postal Reorganization Act, the status quo. We can make some significant changes to the Act, or we can just get rid of it, get rid of the monopoly and have open competition.

Proponents of opening the Postal Service to immediate and total competition overlook one thing, the disruption of the Nation's hard copy delivery system. Our industry just can't afford that kind of disruption. We think that the time for open competition is clearly not now. Legislation with only minor changes would basically be the status quo. DMA believes that if we have the status quo, we will be watching the gradual demise of the Postal Service. That may be the ultimate future for the Postal Service, but we at DMA are not ready to give up on it. So the status quo, we think, is not the answer.

The Postal Reorganization Act needs some significant adjustments. The PMG has stated that he needs more pricing flexibility and the ability to introduce new products more freely more quickly. We agree it is time to give the Postal Service a chance, but giving them this flexibility also gives them the ability to fail and I think it puts a major burden on Congress to hold the Postal Service accountable to make sure that they have, in fact, succeeded and to really take a look at what is going on with flexibility.

DMA recognizes the concerns that people have that the Postal Service may favor one class of mail over another if it is given price flexibility without Postal Rate Commission review. In fact, we have had recent problems with the Postal Service constantly changing its signals and trying to set up a bulk parcel return service, and that reinforces in our minds the need for a Postal Rate Commission. No monopoly should be given carte blanche authority to set its own rates. We think that there is a significant role for the PRC.

The package of legislation that was attached to Mr. Gitlitz' testimony has two major provisions, one giving subpoena power to the Postal Rate Commission and the other giving price flexibility to the Postal Service.

First, the legislation would allow the Postal Service to adjust rates without going to the Postal Rate Commission if its costs are below inflation.

Second, the Postal Rate Commission, not the Postal Service, would determine the postal cost index to see whether or not the Postal Service costs are below inflation.

Third, the Postal Rate Commission must certify that those costs are below the rate of inflation.

Fourth, any rate increase by the Postal Service could only be at 75 percent of the rate of inflation.

Fifth, only one rate increase per fiscal year.

Sixth, all rates must change in the same proportion, and we think that that would eliminate the ability of the Postal Service to favor one class to the detriment of another in these flexible, inflation-driven rate changes.

Finally, it can only last for 5 years beyond the last omnibus Postal Rate Commission decision, so that it would require the Postal Service to go back to the Postal Rate Commission for a full case and thereby there would be some adjustments by the Postal Rate Commission to take care of differences in costs between the classes.

The pricing flexibility that we recommend would be tied to cost control. If the Postal Service didn't control its costs, it does not have the authority to have the pricing flexibility. We think that is the one hammer that we have to try and force the Postal Service to control its costs by increasing productivity and by better managing its resources.

I want to respond to one thing on the fact of: Is reform needed? We think that reform is definitely needed. Without reform, more and more companies will find solutions to controlling their postal costs similar to those that L.L.Bean found and is still finding, using alternative means to interact with its customers. If that happens, the Postal Service and those mailers who can't leave the system, who don't have a viable alternative—many of those in rural America will face higher and higher postage rates with no relief, no help from large mailers, no help from greater volume, no help from growth in revenues, because those large mailers will look elsewhere for other alternatives.

That concludes my testimony. Again, I appreciate the opportunity to be here and I am ready and pleased to take part in our interactive discussion.

Chairman STEVENS. Thank you.

[The prepared statement of Mr. Cerasale follows:]

PREPARED STATEMENT OF JERRY CERASALE

Senator Stevens and Members of the Committee, I am Jerry Cerasale, Senior Vice President, Government Affairs, Direct Marketing Association, Inc. It is an honor to be invited to participate on the closing panel for this stage of your postal reform hearings.

You have already heard the testimony of DMA's President, Jonah Gitlitz, and I support his statement fully and will refrain from repeating his statements. It will be my pleasure to answer any questions you might have on the draft legislation that was presented by Mr. Gitlitz.

DMA commends the Committee for holding these hearings. This is a pivotal time for the United States Postal Service. The Information Age for which we have been waiting for at least a decade appears to be coming to fruition rapidly. How the Postal Service or any universal hard-copy delivery service responds to the information explosion is of great concern to the direct marketers in our nation. The United States Mail is an important link between direct marketers and their customers. At the moment, any disruption in the link would be fatal to many direct marketers.

Therefore, the consequences, both long term and short term, of any postal reform must be considered carefully.

The concern of all users of the Postal Service is that costs and, thus, rates are rising too quickly. Every mailer wants cost inflation to at least slow—absolute decline in costs would be wonderful. How to achieve that goal is where mailers—and the witnesses you have heard today and Thursday—differ. The postal reform legislation which is the goal of these hearings could take three basic forms: Minor changes, if any, to the Postal Reorganization Act; significant changes in the Act; or, elimination of the postal monopoly and creation of full and open competition.

Proponents of opening the Postal Service to immediate and total competition overlook the potential for disruption of the nation's hard-copy delivery network—especially the 180 billion pieces delivered by the Postal Service. The profit margins of most direct marketers is too low to sustain them through a significant disruption in the mailstream. The recent snows in January which crippled a large part of the Northeast disrupted mail service, and the bottom line for many DMA members suffered. The consequences would be much greater if the disruption were nationwide and over a sustained period of time.

Legislation with only minor changes, if any, would keep the *status quo.* DMA firmly believes that if the *status quo* remains, we will be watching the gradual demise of the Postal Service. Postal rates over the past 10 years have increased much faster than inflation; postal productivity despite a huge investment in equipment has not improved significantly; postal costs continue to rise; and new media is bringing new competition into communications. We do not want to stand by and watch our universal hard-copy network wither away. The Postal Service must be provided some incentive to control costs which will hold down rates and make the Postal Service more competitive. The status quo is not the answer.

The Postal Reorganization Act needs some significant adjustments to help the Postal Service face the future. Postmaster General Runyon, following in the footsteps of his predecessors, claims that the Postal Service needs more flexibility in pricing its products and to introduce new products. As Mr. Gitlitz testified, DMA agrees that it is time to give the Postal Service some of that flexibility. Of course, this new flexibility gives the Postal Service more freedom to fail as well as succeed. If Congress does enact legislation to granting the Postal Service more flexibility, oversight of the Postal Service becomes more critical.

Many users of First- and second-class mail oppose any greater pricing flexibility for the Postal Service. They are concerned that the Postal Service will favor other mailers to their detriment. DMA recognizes that fear. No monopoly should be given *carte blanche* authority to set its own rates. We believe there is a significant role for the Postal Rate Commission in any postal reform. The draft legislation that was attached to Mr. Gitlitz' testimony provides for checks-and-balances while giving the Postal Service pricing flexibility.

First, the Postal Service may adjust rates without a Postal Rate Commission proceeding only if its costs are below inflation—not equal to. Second, the Postal Rate Commission—not the Postal Service—determines the index of postal costs through a public rulemaking procedure. Third, the Postal Rate Commission must certify that postal costs are below inflation. Fourth, any rate increase cannot exceed 75% of the rate of wage inflation. Fifth, there may be only one rate increase in a fiscal year. Sixth, all rates must be changed in the same proportion. The Postal Service may not favor one class of mail to the detriment of another. Finally, the authority to set rates without the Postal Rate Commission exists for only 5 years after the Postal Rate Commission has issued an omnibus rate decision.

Thus, pricing flexibility for the Postal Service would be tied to cost control. Without that control, the Postal Service will not have pricing flexibility. We believe that our approach to pricing flexibility protects and even strengthens Postal Rate Commission authority (along with subpoena power) and protects users of each class of mail from discriminate treatment by the Postal Service in the name of pricing flexibility.

The draft legislation also provides that the Postal Service without a proceeding before the Postal Rate Commission may implement experimental postal services which are limited in scope and duration. There are other provisions about which I would be pleased to answer questions but have already been discussed by Mr. Gitlitz.

Any postal reform must be balanced. But reform is needed. Without reform more and more companies will find the solutions to cost control that L.L.Bean faced and is facing—using alternative means to interact with its customers. The Postal Service and those mailers who have no alternative—many in rural America—will face higher and higher postage rates with no relief in sight.

Again, I thank you for the opportunity to appear before you today. It will be my pleasure to answer any questions you may have.

Chairman STEVENS. Mr. Del Polito?

TESTIMONY OF GENE A. DEL POLITO, PRESIDENT, ADVERTISING MAIL MARKETING ASSOCIATION

Mr. DEL POLITO. Actually, I hope God is merciful to you because after the past couple of days, you are going to have to make heads or tails of this. But not to make your life any more difficult, I will try to do what your staff had instructed me to do in terms of offering you comments today, to reflect on what I have heard from others, and perhaps to offer a conclusion on the basis of what I believe I have heard and what I think may be an alternative worthy of consideration.

We have heard from a lot of people about things that we can agree on. We all agree on the idea that the technology is changing and that it will continue to change the way Americans communicate and do business. We all seem to agree that despite these technological changes, the Nation still needs a mail delivery system that is universal, reliable and cost efficient. But there seems to be absolutely no consensus on what needs to be done.

The Postmaster General says that the Postal Service needs to improve its competitiveness. By his very saying so, this implies that the Postal Service is not now competitive and is in danger of being unable to provide universal, reliable and cost-efficient mail service. When I listen to some of the solutions that have been offered, some of the solutions I have offered myself in the past, some of the solutions that have been offered over on the House side, they basically break down into the following.

Some advocate privatization, which includes government's total divestiture of the Postal Service and the abolition of the letter mail monopoly. Some advocate corporatization, which would mean a reforming of the Postal Service into a government-sponsored enterprise with no monopoly. Others, such as the Postmaster General, would advocate commercialization, which basically means let's deregulate the Postal Service, but let's let it keep its monopoly. Others have been before you to say the way to attain the ends that we all seek is to increase congressional and regulatory oversight.

Now, none of these approaches has garnered widespread support, and that should be apparent from everything you have heard over the past couple of days. But in order to be able to craft a rational solution to the Postal Service's dilemma, we really must begin to address at its very heart what is wrong with the Postal Service today.

Now, the conclusion that I have drawn is that the incentives that drive the Postal Service and its employees are anomalous; they are the opposite of what is needed with an enterprise that must operate in a contested environment. Competitive enterprises are driven to minimize costs and maximize gains. The incentives and disincentives that these enterprises have are structured toward fostering those ends. Minimizing costs and maximizing gains are not the driving forces underlying today's Postal Service. The incentives and

the disincentives that exist are not directed toward fostering those ends.

Mr. Volner appeared before you Thursday, sir, and gave you the example of the city letter carriers. The letter carrier who works hard gets more work under today's rules. The letter carrier who doesn't quite work so hard ends up getting rewarded with overtime. The same sort of anomalous incentives exist at the managerial level. Postal managers today are not paid largely in accordance with their ability to trim costs, add new revenues, or generate new business. Their standing within the institution is determined more by the size of the staff that they supervise and the control they have over the operating and capital expenditures budget. These are incentives that fuel costs, not contain them.

Similarly, sufficient disincentives for cost-inefficient behavior simply do not exist. To reform the Postal Service, you must rectify and rationalize the incentives that drive the Postal Service to make them more in tune with those that are more typically found in competitive enterprises. Privatization, suspension of the monopoly, abolition of the mailbox rule are roads toward instilling the Postal Service with a competitive mind set by eliminating those things that originally were designed to insulate the Postal Service from the rough and tumble of the competitive marketplace.

Privatization, corporatization and commercialization, however, are not the only roads that are open for us to explore or to take. Incentives can be restructured in a less radical way that would not require the abolition of the letter mail monopoly or the mailbox rule and would require no major changes to collective bargaining and the binding arbitration processes.

This alternative also could be enough to be able to provide postal management with a way to gain some of the freedoms that they seek from external rate regulation in a way which they say is presently hobbling them through ratemaking, mail classification, the introduction of new products, and the conduct of experiments. This alternative also could foster the concept of postal rate fairness by ensuring that each mail service still pays its attributable costs.

In order to be able to attain this end, sir, what I think would be necessary would be to require in the law that the Postal Service limit its costs and its rates within the bounds of general price inflation. You can mandate that the Postal Service can never raise new revenue in the aggregate in any postal rate proceeding that exceeds the cumulative rate of inflation since the time that rates last rose.

You have to mandate that if the Postal Service can keep rate increases for all mail sub-classes within the bounds of inflation since the time rates last rose and can certify that to the Postal Rate Commission or some other regulatory overseer, it will be allowed to raise its rates up to the cumulative rate of inflation once per year without having its request contested at the Postal Rate Commission. By so doing, mailers can gain a meaningful measure of postal rate predictability, if not stability, in a way that will minimize the disruption of rate increases on their businesses.

The Postal Service could gain annual increases in new revenue that could be used in whatever way the Board of Governors would permit or allow. The Postal Service could gain a measure of regu-

latory flexibility in setting of rates that it presently does not have and seeks through legislative reform.

If you are going to control rates, we must also control costs, so the law would also have to require that postal costs be kept within the bounds of general price inflation. This would be a controlling requirement that would play on the governors, management and all postal workers. While collective bargaining could be permitted under this scenario much as it is today, the parties to bargaining and arbitration would be constrained to ensure that no contract or dispute resolution would have the effect of raising aggregate postal costs beyond projected rates of inflation for the life of the agreement.

Little then would be gained by management or labor by resorting to binding arbitration. The parties would be more highly motivated to come to an agreement that better advanced the institution's long-term competitive needs. There would be no other constraints on pay or benefits provided to management or labor. The controlling influence would simply be the need to ensure that aggregate costs remain within inflationary bounds.

At the minimum, if the system were operated prudently, management and labor could enjoy unprecedented benefits, such as inflation-adjusted wages and salaries. Management salaries also then could be made much more comparable to what exists within the private sector. If the system were even more than prudently managed, they could gain even greater than inflation-adjusted compensation gains in the form of performance-related bonuses, or whatever.

If the costs of the system, however, exceeded or were projected to exceed the cumulative or projected rate of inflation, then management and labor would have to decide between themselves how the costs of the system were to be reduced to remain within inflationary bounds. That might mean they would have to explore adjustments to compensation or work rules or out-sourcing or any other thing that could get those costs within those bounds.

Furthermore, if the Postal Service's costs for each sub-class could not be kept within inflationary bounds, the options available to management would be, number one, determine why the costs for those sub-classes were now out of kilter and what needs to be done in order to pull them back in line so they can continue to enjoy that ratemaking flexibility; or, two, admit a failure to manage costs and services properly and then have to default to the Postal Rate Commission to readdress all service costs and to reestablish new baselines against which future inflation-related adjustments could be made. This, for them, sir, would be tantamount to admitting a management failure, an acknowledgement, I am sure, that they would be loathe to admit and would work doubly hard to be able to avoid because at no time would they be able to go the Postal Rate Commission and either get or have the governors implement rates that would increase revenue in the aggregate that would be greater than the cumulative rate of inflation.

Thank you.

[The prepared statement of Mr. Del Polito follows:]

PREPARED STATEMENT OF GENE A. DEL POLITO, PRESIDENT, ADVERTISING MAIL MARKETING ASSOCIATION

COMMENTS ON POSTAL LEGISLATIVE REFORM

More than a year has passed since Postmaster General Marvin Runyon delivered his landmark speech at the National Press Club in Washington, DC, in which he said that the legislative framework governing the U.S. Postal Service (USPS) no longer was in tune with the nations long-term postal needs. The Postal Reorganization Act, he said, was in need of an overhaul.

Runyon rightly noted that recent technological changes have re-shaped the way Americans communicate and do business, and that these changes have altered greatly the marketplace environment in which the USPS operates. He said that despite its statutory monopoly over the carriage of letter-mail, the Postal Service has been losing market-share in five of its six key markets to alternative providers and alternative media, and that in time it may be difficult to ensure the nation universal mail service under present legislative and regulatory circumstances.

Despite the urgency of the PMG's call for legislative reform, little actually has been done to reform the nation's postal system. Neither postal management nor the Governors have shown an eagerness to describe more explicitly the kind of reform Congress should be asked to consider, while Congress, for its part, has had to focus on other more pressing issues.

Mailers in general have expressed concern over the future viability of the nation's postal service, yet there seems to be no agreement on the form legislative change should take. Indeed, some question whether any legislative reform is needed, and others support only a strengthening of the present regime of congressional and regulatory oversight and control. Despite this lack of consensus, however, virtually all agree that the nation will need for quite some time to come a postal system that can provide *universal, reliable, and cost-efficient Mail delivery services.*

Legislative Reform is Needed.

Recent technological developments within the electronic communication and information arena illustrate quite well the challenges the Postal Service will face in the years ahead. Facsimile, electronic mail (E-Mail), electronic data interchange (EDI), and electronic funds transfer (EFT) already are displacing mail as the primary medium by which businesses communicate and transact commerce. Postal officials have estimated that over the past 5 years the USPS has lost approximately 35 percent of its share of the financial transactions market to alternative media, and will lose an additional 35 percent over the next 5 years.

This diversion of mail to electronic alternatives is a very serious matter—particularly with regard to First-Class mail, which provides approximately 61 percent of all USPS revenue. Business-to-business communications alone account for about 20 percent of the present First-Class mail stream, and it already is evident that a similar transformation has begun to reshape the household/business mail stream.

The number of homes with facsimiles and fax-modem equipped computers has grown phenomenally. A trip to any computer superstore will reveal the love affair many Americans have taken up with computers, and each new sale places in purchasers' hands the tools that are needed to accelerate today's trends.

Consumers have become much more comfortable dealing with electronic communications and transactional devices not only to buy durable goods, but also to provide for practically ever human need. Banks are encouraging their customers to use ATMs in lieu of human tellers for their more routine transactions, and some financial institutions are encouraging their customers to use "smart phones" and PCS to handle many of their transactions at home. Local groceries stores—and even the Postal Service—now accept credit and debit cards in lieu of checks or cash.

The Internet—no longer the play-thing of academics and scientists—has matured into a vehicle for everyday communication and commerce. The World Wide Web (WWW) has made it possible for citizens everywhere to find their way to virtual libraries, databases, and commercial stores. *Cybermalls*, once only a concept, now are a reality.

Twenty years ago, home shopping television did not exist; today, it does. Ten years ago, the idea of interactive television was merely a gleam in a visionary's eye. Few now doubt that within the next decade—particularly with the recent deregulation of telecommunications—interactive modes will transform the way many of us get our information and entertainment and the way we communicate with each other.

As this phenomenon develops, the implications for the U.S. Postal Service will be enormous. The fact is that despite mail's enduring appeal as a communications me-

dium, even a modest change in Americans' communication and business transactional habits can have significant impact on the Postal Service as we know it today.

The Effect of Rising Postal Costs and Rates.

While the cost of communicating and doing business electronically has dropped, the cost of operating the U.S. Postal Service has risen, and seems almost impervious to change. For instance, in 1971, when the old Post Office Department was reorganized by Congress into today's U.S. Postal Service, labor accounted for over 80 percent of all postal costs. In 1996, even after billions of dollars have been spent on the mechanization and automation of mail processing and distribution, labor still accounts for more than 80 percent of postal costs.

This contrasts sharply with the experience of others. For instance, in Canada labor accounts for approximately 60 percent of postal operating costs, and in New Zealand and Australia, labor accounts for 50 percent of total postal costs.

Since the Postal Service must fund its operations from the revenue it raises from its customers, as postal costs rise so also must rates. With each new rate increase, however, the cost of using mail as a business transactional medium will rise disproportionately to the true cost of doing business electronically, which will heighten the demand for nonpostal alternatives.

In many respects, it would appear that the USPS is ill-equipped to deal with its technological competition. Postal managers complain the Postal Service is burdened by overly stringent regulatory constraints, and needs greater regulatory flexibility to enter new markets, develop new products, and price and position its services more attractively within the marketplace. Postal managers also complain the USPS is needlessly encumbered by grievance and arbitration processes than impede productivity, innovation, and cost-efficient operation. Others have chided management for tolerating waste and inefficiency, and for failing to make good on the "promise" of automation.

Plainly, something is wrong with the Postal Service. The only question is: What?

Anomalous Incentives Drive the USPS.

In a nutshell, it's this: The culture of the Postal Service has been driven by incentives that are the opposite of those needed for an enterprise that must make its way within a competitive marketplace. Private sector businesses, for instance, are driven to minimize costs and maximize gains. By contrast, the Postal Service—at least historically—has been driven to do neither.

Despite all the rhetoric about the Postal Service being a "business," it really was never chartered by Congress to be a for-profit, competitively-based enterprise. Rather, it was set up to be what it always has been—an agency of the federal government. As such, the Postal Service is driven by incentives that are characteristic of other government bureaucracies, and minimizing costs and maximizing gains aren't paramount concerns.

Unlike their private sector counterparts, postal managers are not rewarded particularly generously for reducing the enterprise's costs, innovating, or winning new business and revenues. Instead, a postal manager's standing within the organization is determined more by the size of his or her staff or the command he or she exercises over capital and operating expenditures.

The same sort of anomalous incentives can be found at the worker level as well. As former Postmaster General Anthony Frank once described it, if an industrious city carrier completes eight hours worth of work within less than eight hours, the consequence is that the carrier is given more work. On the other hand, if the task is not completed within the appointed time, the carrier gets overtime.

Incentives such as these will not further the Postal Service's ability to survive in a contested marketplace. Indeed, if the USPS is not only to survive, but to thrive, without government subsidies, something must be done to rectify the underlying incentives that shape employees' behavior.

Changing the Incentives.

Those who have studied this matter acknowledge there are alternative ways for instilling the USPS with more market-driven incentives. Some argue that privatization—the total divestiture of government's ownership of the Postal Service, and the repeal of its statutory monopoly—represents the only true path to substantive postal reform. Others advocate corporatizing the USPS into a more business-like government-sponsored enterprises somewhat along the lines of Fannie Mae and Freddie Mac but without the protection of a monopoly. Still others talk of commercializing the Postal Service by relaxing many of the regulatory constraints that govern its borrowing, investing, banking, labor management, and ratemaking functions while

retaining the benefits of its statutory monopoly. To skeptics, however, this sounds all too much like changing the USPS into an unregulated monopoly.

None of these concepts enjoy a wide latitude of support. Each has been criticized as fraught with uncertainties and potentially disruptive to the entire postal infrastructure. As frightful as the prospects of an uncertain future may be, however, the prospects of doing nothing in the face of modern marketplace realities is untenable—increased postal costs, escalating postal rates, increases within key sectors of the USPS' business that exceed the rate of inflation, increased diversion of mail to electronic alternatives, and the eventual need for operating subsidies from the federal treasury.

There is another alternative, though, that could rationally restructure postal incentives, and it could provide management much of the freedom and flexibility it seeks from commercialization. It also could provide postal customers a measure of assurance that mail services could be rendered universally, reliably, and cost-efficiently.

How Can This Be Done?

A transformation to the Postal Service's "culture" could be brought by changing present law to limit the Postal Service's ability to raise new postal rate revenue to an aggregate increase that cannot exceed the cumulative rate of inflation (as measured by CPI–U or some other suitable external and objective measure) since rates last rose. Further, if the Postal Service were able to limit the increases to all its subclasses to an amount no greater than the cumulative rate of inflation, it could be granted the freedom to raise rates annually to an amount equal to the cumulative rate of inflation without having to litigate a rate case before the Postal Rate Commission (PRC). (If, on the other hand, changes in postal costs required subclass rate adjustments beyond the limits of inflation, the USPS either could rectify the causes of any unfavorable cost experience or admit a management "failure" and file an omnibus rate proceeding, much as it does under present law.)

Under such a scenario, the Postal Service also could be empowered to conduct market experiments for a suitable, limited period of time, or introduce new products or services without regulatory encumbrances as long as other postal prices within each mail subclass do not exceed the cumulative rate of general price inflation. In lieu of protracted proceedings before the PRC, management requests for such experiments and new services could be made subject to review and approval by the postal Governors following a period of notice and comment by interested parties

The USPS also could be granted greater freedom over the structure of mail classifications as long as the rates for all affected subclasses were sufficient to recover full attributable costs and make a fair contribution to the recovery of postal overhead costs. Classification requests would be subject to the Governors' approval, and rates for these services still could be subject to Postal Rate Commission review.

Similarly, present postal law could be changed to permit the Postal Service to compensate its employees more flexibly. The only stipulation would be that the aggregate cost of the compensation provided to postal workers—including management as well as labor—could not cause the USPS' total projected costs to exceed the cumulative rate of inflation. Such compensation, however, could be offset by cost efficiency and productivity improvements that could ensure that USPS costs overall remain within inflationary bounds.

Under this "rate and cost cap" scenario, management and labor would be empowered to determine for themselves how work rules, compensation, benefits, or other work-related issues would need to be set to ensure that costs remain within inflationary bounds. This approach would not require changing substantially organized postal labor's ability to bargain in its members' behalf, except for the requirement that aggregate postal costs be kept within inflationary bounds—a principle that would have some controlling effect on collective bargaining and binding arbitrations. There would be an impetus for management and labor to bargain more seriously, since defaulting to arbitration would not necessarily advantage either party. Regardless of whether a contract is derived by collective bargaining or binding arbitration, the mandate still would remain that subsequent postal costs not exceed the rate of inflation. Further, if the Postal Service were prudently operated, workers' pay could be adjusted annually for inflation, or greater, compensation could be provided in the form of performance-incentive bonuses.

What Would Be the Effect?

While mailers might have to contend with the prospect of annual postal rate increases tied to the general rate of inflation, the Nation's recent experience with inflation has been favorable. Undoubtedly, mailers *could* adjust more easily to regularly scheduled postal rate increases of three percent or less per year, which would

be welcome relief from the 25 percent and 30 percent increases that have characterized some postal rate increases of the recent past. In addition, this proposal would not require changes to the letter mail monopoly or the mailbox access rule—a matter of great concern to USPS managers and many mailers alike.

Other Considerations.

The proposal outlined above is merely a skeletal framework for reform. There is much that still needs to be done to fashion a legislative proposal, and there are many issues that still need to be addressed, such as: (1) ensuring that quality of mail service would not suffer as the USPS strives to contain costs, (2) reconciling inflation-related increases with the present policy of setting the single-piece First-Class mail rate in whole-cent integers, and (3) addressing the matter of postal pay comparability. These concerns, however, are not unresolvable.

For instance, concerns regarding whole-cent increases in single-piece First-Class mail need not constrain the pricing of presorted or bulk, presorted, or automated mail, since businesses are quite accustomed to paying fractional rates of postage. One alternative might be to require rounding up or down to the nearest whole cent during years when the resulting percentage would yield a rate increase that is lesser or greater than 500 mills. Another might be to require the USPS to look for ways to improve its cost-efficiency and productivity to ensure that during the years it would get "shorted," it will have a strategy ready to ensure it will still be able to live within inflation-imposed limits.

The matter of pay disparity could be resolved by having the President direct the Department of Labor to study the matter of postal pay comparability and to report its findings to the President and the Congress. These findings, then, could be made a part of any subsequent collective bargaining or arbitration proceedings along with other documents and fact-finding that would serve as background for new contracts.

Who Might Oppose Such Reform?

Conceivably, opposition to such a proposal might come from some mailers, USPS competitors, and possibly even postal management and labor. Some mailers steadfastly believe that productivity gains should be shared equally with mailers and employees. Mailers have expressed concern that a repeat of the runaway inflation of the late 1970s might make living with inflation-adjusted postal rate increases difficult. The truth is, however, that there is no way to indemnify mailers or isolate the Postal Service completely from the adverse effects of economic inflation within the general economy. Consequently, if the nation's economy is managed imprudently, mailers will suffer regardless of whether rates are adjusted under this proposal or under the current scheme.

Competitors of the Postal Service might abhor anything that promises to put the USPS on a more competitive footing. They might fear anything that might improve USPS efficiency and productivity or could make the Postal Service a more formidable competitor.

Some within management may object to being held to a high level of accountability. If the processing and delivery costs of any subclass were to go out of kilter, management would have two options: (1) to recognize that the affected subclass' costs are rising faster than inflation and take corrective action and (2) call for an omnibus postal rate proceeding, which would be tantamount to admitting a management failure.

Finally, there's labor. This proposal would require labor to be more accountable at the collective bargaining table, since all labor agreements would be bound by the need to keep aggregate postal costs within the bounds of inflation. This might go against the union grain. It also might embolden and empower workers to challenge union leadership in matters that workers might not perceive as being in their or the Postal Service's long-term best interests.

In Closing.

These are times of great challenge and change for the Postal Service, its customers, and the nation. Change entails risk, and efforts to expunge all risk—at any cost—may be at odds with the nation's need for reliable, universal, and cost-efficient mail delivery system.

The businesses that rely on the Postal Service's universal mail delivery network deserve more than an endless cycle of intemperate postal rate increases. They deserve a postal system that serves to facilitate, rather than impede, business development and economic growth. They deserve a system that strives to improve the efficiency and productivity of its operations, and pays dividends in the form of improved services and more moderate postal rate increases.

What has been proposed here may seem all too modest and not without its own shortcomings. Nonetheless, it sets forth a framework that may be worth pursuing, even if only to get us on with the serious business of postal legislative reform.

Chairman STEVENS. That is a mouthful.

We don't have any argument, I guess, about universal service.

Mr. DEL POLITO. None.

Mr. CERASALE. None.

Mr. SACKLER. No.

Mr. BRINKMANN. No.

Chairman STEVENS. You have mentioned, Mr. Del Polito, that you have some question about mailbox protection. Do you think that is wrong?

Mr. DEL POLITO. I think the only reason why we have a monopoly on access to the letterbox is because the Postal Service was designed by Congress initially to be sheltered from competition. I don't think you need to abolish the letterbox——

Chairman STEVENS. Of course, the criminal statute was protecting first-class mail, wasn't it? That is where it came from.

Mr. DEL POLITO. Primarily. I don't think you necessarily need the mailbox monopoly in order for the Postal Service to function, but at the same time I don't necessarily think that you need to abolish it in order to be able to ensure its long life.

Chairman STEVENS. You all heard the suggestions of the panel before you that we should address the concept of a postal commission to give the next Congress recommendations as to how to proceed. What do you think about that?

Mr. BRINKMANN. Mr. Chairman, the reality is there are only 40 legislative days, or so, left in this Congress. That is not very much time. In the debate that has gone on, we have heard a lot of suggestions and allegations about the factual basis on which you have got to judge these various proposals, and there is a lot of smoke and not very much fire in some of that.

For instance, the Postal Service continually asserts that it is losing volume. Last Thursday, before the other body, Commissioner LeBlanc submitted a piece of testimony in which he had the following paragraph, if I could read it here for a minute. "If one were to believe the cries of despair from some members of the postal community, one would think that the Postal Service is on the brink of disaster. It is not. Since 1990, total volume for all classes of mail has increased 11.8 percent," and he gives a chart on the back of his testimony that shows that mail volume really isn't declining.

The Postal Service comes in and talks about E-Mail and how it has a declining part of that market and that bodes disaster for the Postal Service. That reminds me a little of an automobile company coming in to you—and the American car companies are doing very well now—and complaining that it is in trouble because it has a declining share of a market that includes all wheeled vehicles in the United States, including buses, trucks, skateboards, roller blades. Just because more Americans are buying skateboards or roller blades does not mean that an American car company is in trouble.

Chairman STEVENS. You disagree with my friend, Mr. Sackler, then?

Mr. BRINKMANN. Absolutely.

Chairman STEVENS. Do you believe that electronic mail is coming and it is a real force in terms of communication for the future?

Mr. BRINKMANN. I think that is coming, but my point is some of that is not a substitute for letters. If I am going to set up an appointment with my boss, for example, about a luncheon, we may send 15 E-Mails back and forth. Some of the E-Mails are 3 or 4 words long. "Is Thursday good with you?" "No." "How about Wednesday?" "No, Wednesday is not good. What about Tuesday? How about 11 o'clock?" That is 15, or 20 little E-Mails. That does not substitute for 15 or 20 letters. Yet Mr. Runyon talks about his universe of E-Mail electronic communications, he is including all those little one-line E-Mails that you send four offices down.

Chairman STEVENS. That is a bad example, isn't it, Mr. Sackler, because, actually, if you are going to bank by E-Mail, it sure is replacing mail?

Mr. BRINKMANN. Banking by E-Mail—I mean, there are different segments of E-Mail and to the degree that banking by E-Mail becomes a substitute for letters in the Postal Service, that is a different issue. That is what I am saying, sir. With only 40 legislative days left, you have to take a hard look at the facts and look at the different types of electronic communications. There is some merit to talking about banking by E-Mail, but in banking by E-Mail, that is also, I would think, fairly price-sensitive. It really does make a difference what the price of a letter is.

Chairman STEVENS. Well, I agree with one thing you say and that is anyone who sat here and listened to all the testimony I have heard, would make up their mind that we couldn't find agreement between the people that have appeared before us, within 40 days. You know, it may well be that the time has passed as far as any reform in this Congress is concerned.

Mr. Sackler, you worry me, though, because when it comes down to these new services, if we got the Postal Service involved in electronic communication now, it would take almost a year to get a rate. Yet, you know this bill we just passed means that you can get into it next month.

Mr. SACKLER. Correct.

Chairman STEVENS. And you set your own rates.

Mr. SACKLER. Correct.

Chairman STEVENS. Do you think the Postal Service can catch up with you?

Mr. SACKLER. No, as a matter of fact.

Chairman STEVENS. I have made my case, right?

Mr. SACKLER. Right.

Chairman STEVENS. What about the rest of you guys? Do you all agree with Mr. Brinkmann? Should we just forget about electronic mail?

Mr. DEL POLITO. No. I can tell Mr. Brinkmann for sure what is happening within the advertising area. I mean, the examples that L.L.Bean gave you Thursday——

Chairman STEVENS. I thought it was fantastic testimony, as a matter of fact.

Mr. DEL POLITO. Absolutely, and people are not going to wait around for things to happen within the postal arena to be able to

address a market that is out there that they need to reach. There are more and more people who are becoming comfortable with doing business online. Technology is going to continue to evolve to make it possible for them to be able to get there, and that is exactly where they are going to be going.

Chairman STEVENS. As a matter of fact, if they complete this new system, Mr. Brinkmann, my *Weekly Reader* that has been going out by mail to every student in the country is going to go electronically within a year. Now, you figure that one out. How are you going to replace that revenue?

Mr. BRINKMANN. I think that is part of the question of getting to some of the underlying facts here, Mr. Chairman.

Chairman STEVENS. I am not talking about getting new revenue from a new service. I am talking about replacing that revenue that has come from mailing things like that, universal mailings almost.

Mr. BRINKMANN. I think that is a problem, because what we are talking about here—when you cut through to the bottom line with pricing flexibility—is shifting costs off of second- and third-class mail and onto First-Class mail; and it is first-class that is going to leave the system first in terms of E-Mail and banking transactions. I don't see how——

Chairman STEVENS. That is not first-class mail. It is a publication like we just had here from Mr. Wendler's people, I think, a similar thing. You have had kids, haven't you? Every one of my kids used to get one of those things.

Mr. BRINKMANN. You know, to the degree that electronic banking transactions would replace mail, I think that would be——

Chairman STEVENS. By the way, they didn't mail them to me. They mailed them to the school, right? You understand that it is not just one little mailing. It goes to a school and then the kids take them home, right?

Mr. BRINKMANN. Yes, sir.

Chairman STEVENS. That is going to be E-Mail soon.

Mr. BRINKMANN. And the second-class that that would replace is an infinitesimal part of the Postal Service's volume.

Chairman STEVENS. But they all add up. Aren't they all straws?

Mr. BRINKMANN. They are. But second-class is, as I recall, only 5 percent of the Postal Service's volume. When you start to lose your First-Class base and the institutional cost contribution that first-class makes to the overhead, that is when the institution gets in trouble.

Chairman STEVENS. Just a little footnote there. It is not going to be too long until all the grandmas are pretty modem-conscious and can handle computers, Mr. Brinkmann.

Mr. Sackler.

Mr. SACKLER. I would agree with that, Mr. Chairman. Certainly, the biggest part of revenues is in first-class. And it would be if there were a huge threat there, and there is one that is growing, where it would be the gravest threat to the system as it exists. But, certainly, E-Mail is not confined to first-class. Again, if we go back to the example I gave you in my testimony of Pathfinder, that is a site where you can find all of our magazines.

Chairman STEVENS. How do you make any money out of that thing?

Mr. SACKLER. We are starting to. As a matter of fact, we have a lot of advertising on it already, and it is growing. I would mislead you if I said it is breaking even yet, but it is getting a lot closer and it won't be all that long. That kind of market exposure to advertisers—27 million folks a week, and growing—is huge, and you can't get by the advertising; it is right there when you first get there, just like in our magazines. So second-class is in play——

Chairman STEVENS. Wait a minute. How is that going to affect the things that go inside Mr. Brinkmann's newspapers? Are you going to replace those inserts that go in the newspapers?

Mr. SACKLER. Well, I think those are largely in competition with third-class mail, with direct marketing.

Chairman STEVENS. I see.

Mr. SACKLER. Direct marketing already is a significant part of the Internet and it is going to grow. Part of the problem here, I think, from those who would have the status quo maintained is that they don't recognize what a dynamic medium the Internet actually is and how much it is changing every day, how much the technology is changing.

Chairman STEVENS. I am sorry to be so abrupt, but that clock is ticking on me. What do you think about this price cap idea? You are supposed to be interactive. What about price caps? You suggested them.

Mr. CERASALE. I think price caps are one mechanism for adjusting rates. One of the questions, I think, that is a big question on it is who determines whether the Postal Service costs are below the rate of inflation to keep those caps, or whatever, and I think that is an area that we recommended the PRC have some role to try and take away some of the fears of Mr. Brinkmann and others that have appeared before you.

Chairman STEVENS. They will become a traffic cop, not a price-setter, right?

Mr. CERASALE. Yes.

Chairman STEVENS. What do you think about that, Mr. Del Polito?

Mr. DEL POLITO. Well, I think the whole idea of cost and price caps is to try and instill within the system, the people that operate the system, the incentives that are necessary in order for them to be able to do the right thing in a competitive environment, and I believe that they serve as a viable route to being able to do that.

I have got one reflection I would like to make on something you——

Chairman STEVENS. Before you get on that, Mr. Sackler, do you agree with price caps?

Mr. SACKLER. Yes. We suggested that, Mr. Chairman. In fact, there is a wrinkle that you can add to them that I understand the FCC applies to some of the regional, if not all of the regional Bell operating companies. When they permit an adjustment for inflation, they also apply what is called a productivity offset, and I gather that is in ranges and the larger the range of offset against inflation that the operating company can select, then the larger the amount of retained earnings it can keep rather than diverting back to its customers because the overall return, the overall rate increase, is going to be smaller for everybody.

Chairman STEVENS. Do you agree, Mr. Brinkmann?

Mr. BRINKMANN. Well, Mr. Chairman, on price caps, I think several things need to be said.

First, with price caps—more than any other specific mechanism—the devil is really in the details. Price caps can vary tremendously, and in that context I think you would have to keep in mind three additional things.

One, since the Postal Service is not a private sector company and since it is a government agency, rates should track costs. If you do a price cap wrong, rates and costs can start to move apart, so you have to do it right.

Second, there is a fundamental issue that would have to be dealt with. It could be a very big problem; or it could not be a problem. And that is with any price cap mechanism—experience particularly in the telecommunications area—has shown that there are significant incentives to degrade service quality. It is not going to do anybody any good if costs stay the same, without increasing productivity, and service deteriorates. That issue would have to be dealt with and it would have to be dealt with very carefully.

Finally, one last point. I actually raised with an eminent economist at the Brookings Institute the concept of price caps on the Postal Service. His response, I think, was interesting and instructive. He told me he would really have to think about the idea for quite a while because price caps were developed in the context of working with a private sector monopoly—a private sector company complete with stockholders and the market pressures and discipline that stockholders create. They weren't really created to deal with a government agency operating in the context of the American economy, and he is really not sure how price caps would work in that context.

So I think that you would have to be very careful with this to make sure that whatever your mechanism you created had the right safeguards built into it, for instance, in terms of service quality. We see the Postal Service more and more pulling out of the public eye its delivery performance data. It is becoming more and more difficult to determine whether Postal Service delivery is getting better, getting worse, or staying the same. There are plenty of stories from one mailer to another, but the hard-core data is disappearing from the public view. A price cap mechanism without full access to delivery data would just not work, among other things.

Chairman STEVENS. Price caps worry me, but you are not as old as I am. I remember when Fords cost $400 and a postage stamp was $.03. Fords cost $22,000 now and the postage stamp costs $.32. You don't have to be a rocket scientist to know that the inflation price cap was irrelevant in terms of pricing of those two products over this period of time.

Price caps might work, in my opinion, Mr. Cerasale and Mr. Sackler, if you had an agreed starting point per product line, but to make them all one-size-fits-all on a price cap, I don't quite see it in this context.

Mr. Del Polito, you were about ready to take us into a new avenue.

Mr. DEL POLITO. Well, first of all, I was going to agree with you. It does need to be done by product line and that would obviously be the first thing that you would have to do before you impose any caps, and that is to go through a regulatory proceeding in order to make sure that everything was done in a manner which was fair and equitable.

Mr. Brinkmann commented about service quality and about rates, and so on. I think the one thing we have got to keep in mind, Senator, is that the conditions that exist today are quite different than the conditions that existed in 1970. I am not so worried about the Postal Service going absolutely bananas with any new-found ratemaking flexibility within the contexts that I have presented them because, unlike in 1970, the Postal Service faces real competition today.

There are viable alternatives for my members to go to to reach the markets that they want to go to and the Postal Service cannot be blind to that competition. So I don't think that that necessarily becomes as great a hurdle for us to come over today as it might have been a quarter of a century ago.

Finally, you said something earlier about whether or not we can afford to wait. The circumstances, I think, that we find in today's environment, sir, are that everyone is talking about reform in one way or another, but nobody has anything on the table. It is like watching planets spin off within the universe because there is no galaxy, no central core, to bring them back in.

I think the moment that you were to lay a bill out on the table, sir, no matter what it looked like, you would immediately find that all of the parties would gravitate around it and begin to push and pull on it to make it work as best it could.

Chairman STEVENS. I would hope that you would be right that they would be pushing and pulling on the bill. [Laughter.]

Mr. DEL POLITO. Undoubtedly.

Chairman STEVENS. Mr. Brinkmann?

Mr. BRINKMANN. Mr. Chairman, one of the points that I made before concerns some of the illusions floating around about some of the underlying facts of the matter, for which I urge the Committee to really take its time and look at the facts. I disagree very strongly with Mr. Del Polito that on the facts of the matter—and this shouldn't be a matter of opinion but of fact—that on the facts of the matter that there is any more increased competition today for hard-copy delivery then there was in past times.

I am putting aside the E-Mail idea and the electronic delivery. But looking at whether his members have any more increased competition—competitive alternatives—to the Postal Service than they used to, I just don't think that there is anything of any real significance. Indeed, one of the two alternate delivery companies just went out of a business as a result of the reclassification case, and the Postmaster General in a recent speech somewhat gloated at that.

Mr. DEL POLITO. I take little comfort in Mr. Brinkmann's assurance on current mail volumes, and so on. As you well know, in Anchorage, sir, the earth is always still before the quake comes. The weather always seems nice before the storm.

Chairman STEVENS. You feel the rumble.

Mr. DEL POLITO. Well, that is just it. I think if we take a seismic reading of our postal system, sir, we will probably get a better idea of what actually is awaiting the Postal Service.

Chairman STEVENS. Mr. Sackler?

Mr. SACKLER. Mr. Chairman, let me just respond for the record because it was our alternative delivery company that just closed up shop. Now, it wasn't a result of the Postal Service's reclassification case that it closed up shop. In part, it was because of improved performance by the Postal Service over the past few years, but in major part it was because we did not have access to the mailbox. I hasten to say we are not advocating any change in that before you today.

Because we could not get into the mailbox, consumers were not happy. They were not happy with receiving magazines or other mail in their driveway, at their doorstep, on a door knob, or any other way. Even though newspapers do that every day, they didn't want to see anything but newspapers in their driveway, and so that was the reason ultimately, because people would complain and shift their attention elsewhere, that we ended up closing shop. So it is not the way that Mr. Brinkmann characterized it.

Chairman STEVENS. Mr. Cerasale was next.

Mr. CERASALE. One of the things that I have to disagree with Mr. Brinkmann on is that if you look at L.L.Bean, it started its Website in January and it cannot keep up with the demand right now in March. It is not hard copy delivery where the competition is; it is the idea of our members and direct marketers meeting the needs of their customers through another mechanism and just abandoning the Postal Service altogether.

Postal volume may be rising and has risen since 1990, but when you look historically at where postal volumes have been and look at how the economy has come, postal volumes are not growing as robustly as they should in comparison to the growth of the Nation's economy over the past 3 years. That is a warning sign. That is the little rumblings that you feel before the earthquake. I think the signs are there.

The Postal Service's strength in volume growth, which is what helps keep rates down by spreading the cost of this nationwide delivery network—that growth is not materializing. It is not materializing in third-class and it is not materializing in first-class mail, and that is a real problem and it is a sign that says something has to be done, and something has to be done rather quickly.

Chairman STEVENS. Well, you know, I went to the demonstration of the wedding between cable and telecommunications—telephones, primarily—to announce that they were going to wire every school in the country for computer training, and I felt the rumble. The rumble is those kids are going to be computer-capable and modem-capable by the sixth grade and they are not going to be writing grandma. They are going to be using telecommunications, E-Mail, and I think those people who are involved in those businesses are very wise in what they are doing. They are making an investment in the future, and it is communications, Mr. Brinkmann. It will be newspapers, too, soon.

There has been that experiment in Japan, as you know, and you can pretty soon see people getting the sports page of the San Fran-

cisco paper and the editorial page of the hometown paper and getting no advertising other than what they ask for. I believe you should listen to Mr. Sackler a little bit about the future of the Postal Service because the competition is just there. It is just right around the corner and there is liable to be a cliff there for the Postal Service to fall off if we are not wise in how to handle it. I see my friend back there shaking her head, but I still think there is tremendous competition out there.

I want to ask you one last question. Everybody who has been here has talked about the dynamic aspect of the American communications system. Do you all agree that it is dynamic out there?

Mr. CERASALE. Yes.

Mr. SACKLER. Yes.

Chairman STEVENS. What is dynamic about an institution that takes at least 10 months to change the rates? Tell me that. What is dynamic about this system? How can we say they can participate in a dynamic society if it takes more than 10 minutes to change the rates to meet the competition?

Mr. SACKLER. It is even more than that, Mr. Chairman. It takes them several months to prepare a case and then there is the month or two that the governors have it after the fact. So we are talking about a year-and-a-half.

Mr. CERASALE. That is right.

Chairman STEVENS. I am not saying it all has to go away, but isn't there—I am implying a question—isn't there room here? Isn't there a need for some change to make sure we preserve the postal system?

Mr. BRINKMANN. Mr. Chairman, I think the problem is—and let me correct something for the record. We understand, clearly, that the growth of electronic communications, E-Mail, electronic banking, electronic newspapers, electronic catalogs, will significantly impact the Postal Service. Indeed, I suggest to you that it is clearly the number one public policy issue of the next 5, 6, or 10 years in the postal area, just as it will clearly have a major impact on newspaper publishers.

Our publishers don't think that anything of any significance is going to happen in the next 4 or 5 years. Many question whether it will happen in the next 5 to 10. It will clearly happen, they think, after that.

The problem here is the relationship between the so-called pricing flexibility concept and the electronic growth of communications. That is the problem.

Today, the Postal Service is a monopoly. It, in essence, can't lose money because it has control over its own revenue requirements. There is no check and balance on it. It doesn't pay taxes. It is immune from the antitrust laws. All of this business in telecommunications started back in 1956 when the Justice Department walked in and sued AT&T with an antitrust lawsuit. That can't happen to the Postal Service. There simply isn't that mechanism.

We are talking about a much, much different animal. To talk about pricing flexibility in that context, I think, means you have to look at its relationship to these growing electronic alternatives and, consider the nature of the beast, which is fundamentally dif-

ferent than private sector companies competing in an environment where technology is changing on a rapid basis.

There is no suggestion today that the fundamental cost of delivering a letter or a package or a catalog or a magazine—which is cars, gas and wages—is going to decrease by 70, 80 or 90 percent in the next 10 years. That is what has happened in the telecommunications industry. That is what is going to happen in the future of the telecommunications industry. A computer that cost $1 million when I was in college—which wasn't that long ago—now costs, at best, less than $100, and that is the switching mechanism of the telecommunications industry.

They are fundamentally different industries, Mr. Chairman, and the technology changes happening in telecommunications are not happening in the Postal area. Indeed, the question I think that you have to ask at some point is if indeed these electronic alternatives really do grow as much as people think they will, in 10 or 12 years what role will the Postal Service have in our society and what will be the need for a postal service?

Will the person in Nome, Alaska—what will be their need? If they can get the *New York Times,* the *Wall Street Journal,* instantly over a computer line, if they can order catalogs from whatever mailers they need over a computer line, if they can send E-Mail instantaneously to anybody in the world, what will be the role of the Postal Service in that view? I mean, clearly, they won't be able to get a parcel over the line, but beyond that, what will the Postal Service be doing? That is a fundamental question that nobody has really addressed in this context.

Chairman STEVENS. That is precisely what we are trying to answer.

Mr. Sackler.

I am just going to go down the table now and then wind up.

Mr. SACKLER. Well, Mr. Chairman, I would agree with Mr. Brinkmann's premise that the Postal Service and all these new communications media are fundamentally different. I would profoundly disagree with his conclusion. They are, in fact, competing. That competition will grow more intense and the Postal Service will only be able to find its way if it can respond in some rapid fashion to the various kinds of products, commerce, shopping, banking, news, and everything else you will find on that new communications media in order to retain its basic character as a coherent institution to serve the public.

Chairman STEVENS. Mr. Cerasale?

Mr. CERASALE. Mr. Brinkmann's view of the Postal Service in 10 years may be true, but I think the conclusion he comes to is wrong. We have to then give the Postal Service a chance. If we don't make some changes, the Postal Service doesn't have a chance to survive. I think in the next 40 days, your idea of taking some first steps is what is needed. I think, as you look at it, take some steps to give the Postal Service a chance. That doesn't mean we don't look in the next Congress at more steps.

As you are looking at it, try to consider some of the fears that you have heard from the newspaper people and some of the first-class mail users and other second-class mail users and try and put some protections in in the short term to alleviate some of their

fears, but start on the road and give the Postal Service some chance, and let's test them. Let's give the Postal Service a chance to make it. They may fail, but if we don't do anything, most likely they will fail anyway.

Chairman STEVENS. Mr. Del Polito?

Mr. DEL POLITO. In the midst of changing times and changing technology, sir, there is not going to be any manna from heaven that is going to fall down in order to be able to save the Postal Service. So we have to wake up to the reality that, in fact, things are changing and it will impact on the postal system.

Yes, the ratesetting process is a very painful one for everybody that is involved, but I think that if we adjust the incentives the appropriate way, postal management and labor will do everything that they can to make sure that the visits they have to make at the Postal Rate Commission are as infrequent as possible.

Chairman STEVENS. Well, thank you very much. You know, I am worried about this commission proposal. It may be that the Congress and the general public wants us to create a commission and we will do it. The earliest date it could lead to legislation would be 1998. There is no way you can get a commission created and have it report back and get action before 1998. I still have the feeling that there is going to be substantial change.

I see good friends out there in the audience and I would just like to remind them that when I went home last November, on my birthday I found two birthday cards on my pillow. They both were transmitted from Alaska by telecommunications and had been made up on a computer by my grandchildren. Now, the future is here now, right now, and I think unless people recognize where the competition is, we are just not going to have a postal system the way that I envision it to be needed in the next century.

So we are still going to get two drafts out, aren't you, staff? Before the recess, we will have the draft for the commission and the draft for my suggestion for some reform now.

Thank you very much. I appreciate it.

[Whereupon, at 3:55 p.m., the Subcommittee was adjourned.]

APPENDIX

PREPARED STATEMENT FROM DAVID C. TODD, COUNSEL FOR MAIL ORDER ASSOCIATION OF AMERICA

PATTON BOGGS, LLP
WASHINGTON, DC
March 21, 1996

The Honorable Ted Stevens, *Chairman,*
Governmental Affairs Committee
Dirksen Senate Office Building
Washington, DC.

DEAR SENATOR STEVENS: This statement is submitted on behalf of the Mail Order Association of America (MOAA) with the request that it be included as a part of the record of the hearings concerning possible amendments to the Postal Reorganization Act which you have held over the past several days.

Members of the Mail Order Association of America make extensive use of first-class, third-class, and fourth-class mail (Standard Mail) and as such are vitally interested in a properly structured and efficient mail service.

It is the position of MOAA that the Postal Service will not be able to carry out its function properly in the absence of significant changes in the relationship between the Postal Service and the Postal Rate Commission. The 1970 Senate report, leading to the adoption of the provisions of the Postal Reorganization Act creating the Postal Rate Commission, observed:

> If a bureaucratic struggle between the Board and the Commissioners develops, then the whole theory of independent ratemaking judgments will have failed and the Congress will probably be called upon to revise the system.

Unfortunately, the "bureaucratic struggle" between the USPS and the PRC feared by the Senate has in fact developed.

The PRC has become an obstacle to bringing about the kinds of structural changes that are needed if the Postal Service is to be able to continue to compete in existing and emerging market environments. In their the March 4, 1996 Decision in the recently concluded classification reform proceeding, the Postal Governors found that "the Commission has focused more on reasons to decline to recommend progress, and has been more vigorous in pursuit of the status quo, than it has in a search for solutions to the fundamental challenges faced by the Postal Service, its management, and its employees" Governors Decision at 21. MOAA concurs with that finding. MOAA also agrees with the Governors' conclusion that despite some positive results from the classification proceeding, there needs to be legislative improvement in the processes. As stated by the Governors, "the loose jumble of statutory classification and ratemaking factors applied in these proceedings gives the Commission broad opportunities to attempt to foist its own policy judgments on the Postal Service" Governors Decision at 22.

MOAA recognizes that so long as there are monopoly services, it is essential that an independent Postal Rate Commission continue to exist for the purpose of recommending postal rates. MOAA also believes, however, that proper classifications are essentially of a management nature and that the Postal Service should be given substantially greater freedom to establish classifications as it deems to be appropriate. MOAA believes that the absence of greater Postal Service classification authority inevitably will result in a deterioration of the ability of the Postal Service to serve the mailing needs of the country.

Further to these objectives, MOAA recommends the Postal Reorganization Act be amended to provide authority to the Postal Service to classify its services in accordance with its management judgment as to how those services will best meet its ex-

isting and future operational requirements and the realities of the marketplace. Such authority would require that the Postal Service establish rates for such classifications that are sufficient to ensure that each class or subclass of service would generate sufficient revenues to meet all of its attributable costs plus a reasonable proportion of other costs in order to meet the institutional burden of the Postal Service. Further, the Postal Service should be required to submit the rates for any new class or subclass of service to the PRC for approval within a specified period of time.

MOAA also supports changes to the Act which would give the Postal Service greater authority to establish rates. Specifically, MOAA supports the following changes:

1. Provisions should be adopted giving the Postal Service authority to establish rates for competitive services within bands of rate freedom as established by the Commission. Thus, for competitive services, the PRC at the request of the Postal Service would be required to establish both minimum and maximum rates for competitive services, within which the Postal Service could price as it deems market realities require.

2. The Postal Service should be given authority to enter into negotiated contract rates with mailers provided that any such rates would be required to meet all attributable costs and a reasonable portion of the institutional costs of the Postal Service. This is the kind of authority which is already enjoyed by Postal Service competitors such as the United Parcel Service, which has enabled such competitors to meet market realities in a way which has been denied to the Postal Service.

3. The Postal Service should be given the authority to raise or lower rates subject to an indexation formula under which would the Postal Service could raise rates to the extent that neither costs nor rates exceed the indexed rate of inflation. Under such a system, there should be a requirement that rates be submitted to the PRC for approval at stated minimum intervals.

4. The Act should be amended to require the Commission to give greater emphasis to demand in the pricing of postal services, as has been recommended by the General Accounting Office. As has been recognized by the GAO, demand pricing which would maximize volumes for those services which are most price sensitive, would benefit all mailers since it would ensure that there was a maximum volume to meet the institutional costs of the Postal Service.

5. PRC Commissioners should be appointed from a panel of nominees from selected appropriate groups such as the American Economic Association. The House version of the 1970 Act contained such a provision and the House report explained that the procedure would assure "insofar as practical, that appointments would be made on the merits and without political favor from respected professional experts whose qualifications have been established by their service either within or without the government." MOAA believes that such a process would help to ensure that the Commission would not be excessively politicized, which was one of the primary purposes for creating an independent Commission in the first place.

6. The Act should be modified to provide that the full Board of Governors could modify Commission decisions with the support of 75 percent of the Board and without requiring that there be a finding that modification is necessary in order to meet the break even requirement of the Act.

We appreciate your consideration of these views and would be pleased to discuss any questions which you or your staff may have.

Sincerely yours,

DAVID C. TODD,
Counsel for Mail Order Association of America

LETTER SUBMITTED FROM AVANTI PRESS, INC.

AVANTI PRESS, INC.,
DETROIT, MICHIGAN
March 8, 1996

The Honorable Ted Stevens, *Chairman*
Subcommittee on Post Office and Civil Service
U.S. Senate
Washington, DC.

DEAR MR. CHAIRMAN: I understand that the Senate Subcommittee on Post Office and Civil Service has begun a series of hearings to determine whether reforms are necessary to the U.S. Postal Service. I am writing to express my views on behalf of my company, AVANTI Press, Inc., and in conjunction with the Greeting Card Association, of which I am a member.

I want to compliment you and the committee for undertaking this task. As I do in my own business, I believe it prudent to look at what changes might be required to keep it healthy and growing. Certainly the USPS must look at those same issues. After completing that review, the question then becomes, "Do changes really need to be made?"

In my opinion, the USPS must remain customer friendly. From my standpoint that means it must, first and foremost, take into account the effect of any of its actions on "Aunt Minnie". She really has no voice in these debates (other than through the GCA), even though she is guaranteed that right in the mission of the USPS. It appears to me that the safeguard to her protection is through the watchdog authority of the Postal Rate Commission. If the USPS wants to maintain such paper-based communications as we know them today, it, too, will want to treat its loyal customers favorably.

I am certain there are many other advancements that the USPS could undertake to advance the interest of "Aunt Minnie." I know that you and the other members of your committee recognize the importance of maintaining cost effective delivery of First Class mail for your constituents.

I congratulate you for taking on this task, and look forward to communicating with you on these issues as you begin to formulate responses to the questions you have so appropriately raised.

Sincerely,

CHIP OWEN,
Vice President

LETTER SUBMITTED FROM POPSHOTS, INC.

POPSHOTS, INC.
WESTPORT, CONNECTICUT
March 8, 1996

The Honorable Ted Stevens, Chairman
Subcommittee on Post Office and Civil Service
U.S. Senate
Washington, DC.

DEAR MR. CHAIRMAN: As a member of the Greeting Card Association, I am pleased to provide input to the subcommittee's hearings on "USPS Reform—Conversations with Customers."

As part of the greeting card industry and as president of a company whose business relies on the mail as a vehicle for delivering much of its product, I consider us partners with the United States Postal Service. We need a strong and viable Postal Service that can meet the challenges of the future—and one that continues to meet its mandate for universal mail delivery.

Nearly two-thirds of all greeting cards are mailed, and we believe the core of hard copy, which would include all other household-to-household mail, will not be diverted from the mailstream. Our joint goal is to increase volume of this mail by sustaining a Postal Service that is consumer friendly.

In doing this we believe the Postal Service must remain true to its mandate that a vigorous Postal Rate Commission be maintained. By affording the citizen mailer with protections against unnecessary postal rate increases or other intrusions into the universal mail delivery standard, the USPS can provide additional benefits to citizens. One such example could be to have the Postal Service begin studying how it can foster the use of bar code technology in households.

We stand ready to work with the Postal Service to meet its challenges for they also are our challenges. We appreciate the subcommittee's interest in this important issue.

Sincerely,

PETER VAN WITT
President

LETTER FROM MR. GLEIMAN, CHAIRMAN, POSTAL RATE COMMISSION

POSTAL RATE COMMISSION
WASHINGTON, DC.
March 18, 1996

Honorable TED STEVENS, *Chairman,*
Subcommittee on Post Office and Civil Service,
Committee on Governmental Affairs,
U.S. Senate,
Washington, DC.

DEAR MR. CHAIRMAN: Although I was unable to attend your March 14 hearing on postal issues, the hearing was broadcast on C–Span and I was able to watch a video tape replay. One witness, Timothy J. May representing the Parcel Shippers Association, mischaracterized my testimony before the House Subcommittee on the Postal Service, and misrepresented the Postal Rate Commission's recommended decision in the recent classification reform case. I respectfully ask that by this letter I be permitted to respond to Mr. May's comments and that this response be included in the hearing record.

First, Mr. May complained that, at the March 13 hearing before the House Subcommittee on the Postal Service, I devoted my entire time to the courtesy envelope mail (CEM) issue. Enclosed is a copy of the statement I presented to the Subcommittee. About 2 of 12 pages addressed CEM. As you can see, it was only one of many matters discussed. At the hearing, the issue was first raised by Chairman McHugh in a question to the Postmaster General. During my appearance, again it was only one of many issues discussed. Mr. May may believe it is inappropriate for me to respond to certain questions from the Chairman of a subcommittee of competent jurisdiction. If so, I do not share his view.

Mr. May asserted that the Commission's CEM recommendation was a proposal for a "deeply discounted" rate, and said there would be a 12 cent discount. Wrong again. The Commission recommended CEM as a "shell" classification, and asked the Postal Service to propose an appropriate discount. As the Commission decision notes: "The Commission will recommend the CEM category purely as a mail classification concept for the Governors' consideration, and it will leave recommendation of a specific discount to a subsequent ratemaking proceeding." PRC Op. MC95–1, para. 5084.

Similarly, since the Commission recommended CEM only "as a mail classification concept for the Governors' consideration," Mr. May's additional complaint that CEM's "principle beneficiaries would be a few large companies like American Express" who provide postage paid envelopes could easily be remedied. This mail is commonly called business reply mail and is subject to special handling and fees. If it were eligible for the CEM discount it would comprise a small percentage of mail in the CEM category. But if this troubles Mr. May he could urge the Governors to exclude this mail from the CEM category. It would be within the power of the Governors to make such a recommendation, although if this mail is cheaper to handle, it seems perfectly appropriate to accord it the discount.

It is clear that Mr. May either had not read the Commission's decision, or if he had, did not understand it.

I commend you for your efforts and interest in improving postal matters. You received many interesting suggestions and recommendations for changes in the Postal Reorganization Act. The Postal Rate Commission, also, will be providing some suggestions, and would welcome the opportunity to comment on legislative proposals as they are developed.

Sincerely,

EDWARD J. GLEIMAN

Enclosure
cc:
Senator David Pryor
Senator Bob Smith

Representative John M. McHugh,
Chairman, Subcommittee on the Postal Service
Mr. Chris Rebello,
President, Parcel Shippers Association
Mr. Timothy J. May, Esquire

PREPARED STATEMENT BY EDWARD J. GLEIMAN, CHAIRMAN, POSTAL RATE COMMISSION BEFORE THE SUBCOMMITTEE ON THE POSTAL SERVICE, COMMITTEE ON GOVERNMENTAL REFORM AND OVERSIGHT, U.S. HOUSE OF REPRESENTATIVES

MARCH 13, 1996

Chairman McHugh, Ranking Member Collins, and Members of the Subcommittee: Thank you for inviting me to testify. I am accompanied by my colleagues Vice Chairman W.H. "Trey" LeBlanc, Commissioner George W. Haley, and Commissioner H. Edward Quick, Jr.

I have much to report. Since last we met, the Postal Rate Commission has been very, very busy. Last June, after a request from the Postal Service Governors, we issued our Opinion and Further Recommended Decision in Docket No. R94–1, the most recent omnibus rate case. That decision was adopted by the Governors. We have considered and completed a major mail classification reform case, Docket No. MC95–1. Since December 19, 1995, we have been considering the Postal Service's request for expedited consideration of an experimental case involving First Class and Priority small parcels. And, we have made significant progress in Docket No. RM95–4, a rulemaking proceeding intended to provide further streamlined procedures for certain types of cases. I will have more to say on that in a few minutes.

We have modernized the Commission's computer systems, with a view toward facilitating data transmission and, eventually, electronic filing. I want publicly to thank the Postal Service for its technical assistance in this regard. Recently I wrote the Postmaster General asking his assistance to simplify further our proceedings by ensuring that all data filed by the Postal Service is presented in a standard format. Also, in its reclassification decision, the Commission announced its intention to launch a rulemaking proceeding to reexamine its "computer evidence" rules.

As a result of your initiative, Mr. Chairman, we are working with the Subcommittee, the Postal Service, and the General Accounting Office (GAO) to study how the information and data needs of the ratesetting process can be better served. I thank you for moving forcefully to address the concerns I expressed about this when I appeared here last year. We have also, on several occasions, provided technical assistance to the GAO, most recently in connection with its study on international mail, released this week, and its work concerning the Private Express Statutes.

Despite this progress, we continue to be concerned about the expense and effort required of parties who participate in major rate and classification cases. Now that the classification case is completed, we hope to open discussions with various parties to explore methods to reduce the effort and expense required to participate in rate and classification proceedings.

In the midst of all of this, we have disposed of an unusually large number of small post office appeals. We also, in February 1995, initiated a rulemaking proceeding to amend our rules of practice to provide that a post office appeal is timely if the appeal was *postmarked* before the 30-day time limit. Our existing rule requires the appeal to he *received* by the Commission within the 30-day time limit. On March 30, 1995, the Postal Service filed comments opposing the proposed change, arguing that the Commission does not have the statutory authority to make such a change in its rules. We have held this proceeding in abeyance while related legislation is being considered in the House, but a statutory change is probably desirable. Mr. Chairman, I know the Subcommittee is familiar with this type of issue, where practice under existing law sometimes appears inconsiderate of overall equity and fairness.

We have accomplished the above despite the fact we have fewer staff today then when I appeared here last March; and, our budget, when adjusted for the one-time purchase of computer equipment, has not grown by even one penny.

The mail classification reform case, MC95–1, was a huge effort, not just for the Commission, but for the Postal Service and the many interested and affected parties. The case affects 89 percent of all mail volume. Most rates for this mail will change because of the restructuring of the mail classification schedule.

We were very pleased the Governors, with two exceptions, accepted our recommended decision in the reclassification case. One of the exceptions, the "bulk par-

cel" issue, is a very technical matter, and we disagree with the position taken by the Governors.

The second exception, involving Courtesy Envelope Mail (CEM) deeply troubles me, and I will touch on that in a few minutes. First, an overview of the decision.

The case was completed in the ten months contemplated by the law (plus three snow days). More than 70 parties participated, and the Commission held 35 days of public hearings. The transcript comprises more than 17,000 pages. Now, I know there are some who say this process is too long and too complicated. But, please consider that the mail affected by this case generates 80 percent of postal revenues—that is $43.7 billion. A change in rates of a few tenths of one cent means millions, maybe even tens of millions, of dollars to a major mailer. Even changes that do not involve large amounts of postage, such as changes in mail eligibility requirements, can have a profound effect on mailers whose livelihood depends on access to the postal system. The stakes are extremely high. It is critical that affected parties be permitted to participate in a meaningful manner, and, frankly, that requires some time and great care. As one of our lawyers recently said to me, "sure, we can speed up this process. It's just a matter of whose due process rights you want to take away!"

This was the first comprehensive look at mail classification since the 1970 enactment of the Postal Reorganization Act. The Postal Service and the parties advanced numerous classification theories, often competing or conflicting, to justify mail classification changes they proposed. In the end, the Commission's Opinion sets forth clear guidance for applying the statutory classification and ratesetting criteria (39 U.S.C. 3622, 3623). It recognizes that the function of mail classification is to create groupings of mail *for the purpose of ratemaking.* Under the Postal Reorganization Act, and judicial and Commission precedents applying it, postal ratemaking involves two fundamental steps: (1) the attribution of direct and indirect costs required by 39 U.S.C. 3622(b), and (2) the assignment of institutional, or overhead, costs in accordance with the noncost criteria set forth in the statute. The attributable costs comprise 65 percent (more than $36 billion) and the overhead costs about 35 percent (about $20 billion) of total costs.

The Commission recommended the renaming and regrouping of existing mail classes as the Postal Service requested. Express Mail will become Expedited. First-Class Mail will be unchanged, but existing third and fourth class will be combined into a new Standard Mail class. Existing second class is renamed Periodicals class.

The Commission endorsed the Postal Service goal of promoting automation by restructuring classifications and rates to reward "workshare" mailers. These mailers prepare mail for processing on automated equipment and mail that otherwise bypasses postal operations, thereby reducing postal costs. Many of these mailers will see rate reductions which reflect their worksharing activities.

The Recommended Decision encourages automation-compatible mail.

The Commission largely adopted the changes in mailing rules and procedures proposed by the Postal Service in the form of a new Domestic Mail Classification Schedule, thereby permitting the Service to go forward with the 123 Federal Register pages of implementation rules it had developed in consultation with its customers.

Probably the most controversial aspect of the Postal Service's proposal pertained to second-class mail—mostly magazines and newspapers. The Postal Service proposed dividing the existing second-class regular subclass into two new subclasses with, essentially, one for large publications and another for small. Opponents of this proposal argued that it would lead to an unfair allocation of postal overhead costs, thereby harming many for the benefit of a relative few. The Postal Service's proposal would have meant an average 17 percent postage *increase* for more than 11,000 small volume periodicals to effect an average *decrease* of 14 percent in rates for some 800 densely-circulated publications.

The Commission rejected the Postal Service's subclass proposal for magazines and newspapers. It could find no basis, economic or otherwise, for drawing such an arbitrary line between large and small publications. It did, however, recommend rates that reflect the worksharing activities of publication mailers. Large, highly-presorted publications (the roughly 800 identified by the Postal Service) will experience an average rate decrease of 3.7 percent, not 14 percent. The average increase for others will be 3.5 percent. Improved Postal Service cost studies in this area could lead to further rate refinements.

The Commission endorsed a Postal Service proposal for a new Enhanced Carrier Route subclass in Standard Mail and has been harshly, but understandably, criticized by some competitors of the Postal Service for this action. While we wish we could please everyone, we, of course, cannot. We have a law to follow and apply to the facts presented in our proceedings. As the Commission's decision explains, the evidence clearly supported dividing carrier route and noncarrier route mail into sep-

arate subclasses. The concern of competitors (primarily large daily newspapers) is understandable because the new subclass results in lower rates for mailers who compete with them for advertising dollars.

I mentioned the Governors' rejection of the CEM recommendation. This is why their action troubles me.

First, what is CEM? CEM, as recommended by the Commission, is limited to preprinted reply envelopes provided to consumers by entities expecting or hoping for remittance mail (for example, credit card or utility companies sending bills, catalog companies distributing mail order forms, or charitable organizations seeking donations). This mail, although generally deposited one piece at a time by householders, can he sorted directly by automated equipment because it displays both a preprinted barcode and a Facing Identification Mark (FIM). Also, it is frequently picked up at the post office, avoiding the need for delivery. Thus, it costs less to process and should be eligible for a discount.

The Governors' decision complains that the CEM recommendation was not based on a recommendation "proposed by the Postal Service in this proceeding." This is true. But, the Commission's Office of Consumer Advocate proposed this classification, and the Commission thought the evidence demonstrated the need for it. CEM is important because it has the potential to touch each and every person in this country who pays a bill by mail.

Exactly one year ago today, the U.S. Postal Service issued its Press Release No. 23, entitled "Customers Get First Look At Reclassification Case." Let me read you a short paragraph from the third page of that release:

> The Postal Service will also propose that reply envelopes included in the First-Class automation subclass be properly barcoded. The Postal Service plans to ask the Postal Rate Commission at a later date for a lower rate based on the lower costs of automating this mail. These savings would be passed on to the consumer.

Mr. Chairman, when the Postal Service makes such a public commitment, should not the public be able to take the Service at its word? Apparently not.

One of the Postal Service mottoes is "We Deliver for You." The Commission's decision gave the Service the opportunity to live up to that motto. We recommended a "shell classification" and left it to the Postal Service to fill the shell, as it saw fit—as one year ago it publicly said it would.

And, what did the Postal Service Governors do? With great gusto and a number of, at best, specious arguments about operational problems—problems that simply do not exist by virtue of establishing a shell classification, they ground the shell to dust. They threw out the framework needed to do what the Postal Service told the public, in its Press Release No. 23, it was committed to doing.

In recent weeks Postmaster General Runyon has been talking about threats to First Class mail volumes from technologies—for example, the potential growth in electronic bill paying by individuals. This mail is CEM or courtesy envelope mail. This is the very mail that would have been the beneficiary of those savings that were, according to Press Release No. 23, going to be passed on to the consumer. Perhaps fulfilling the commitment made in Press Release No. 23 would help keep in the system the very mail about which the Postmaster General is worried.

I hope that the lone dissenting voice among the Governors on this CEM issue, that of Governor David Fineman, is enough to ensure that individual mailers will soon get the benefits promised a year ago. But even if this should come to pass, I still will not understand why the Governors took the action they did in rejecting the CEM shell. Their action makes no sense at all, unless they never really intended to let the general public share directly in the benefits of automated mail.

Last year, when I appeared before the Subcommittee, I suggested, partly in response to the Postmaster General's call for more flexibility in setting rates and introducing products, that the Postal Service reexamine the recommendations of the 1992 Joint Task Force on Postal Ratemaking. Shortly after that, I met with the Postmaster General, then Chairman Winters, and other Governors and urged this course of action. So, I was pleased when the Postal Service, shortly after our meeting, petitioned the Commission for rules based on the Task Force's recommendations. The Commission promptly initiated a rulemaking proceeding (Docket No. RM95–4), and has had two rounds of comments on various aspects of the Postal Service's proposal. The initial invitation for comments on the Postal Service's proposals drew diverse comments from 21 parties.

In response to these comments, last October the Commission published proposed rules to implement a majority, but not all, of the Postal Service's procedural initia-

tives.[1] The Commission explained it was proceeding in this limited fashion for several reasons. First, it was mindful of the current workload imposed on all those involved in Docket No. MC95–1 and mail classification reform generally. Second, there were potential legal impediments to implementing at least some of the rules held in abeyance. And, finally, the four initiatives for which proposed rules were published appeared "to hold the greatest promise for procedural reform in the near term."[2] The Commission promised, however, that it would "endeavor to pursue the remaining initiatives, which appear to present somewhat greater challenges under the Postal Reorganization Act as currently interpreted, in subsequent proceedings."[3] Frankly, we thought this was the most expeditious way to proceed. We would tackle the seemingly less controversial proposals first.

Well, when it comes to the Postal Service, as I am sure the Subcommittee has learned, very little is noncontroversial. In the 17 sets of comments submitted, the Commission was criticized both for what it proposed and what it did not propose. One party went so far as to assert that the Commission's failure to address immediately the negotiated service agreements or "contract rates" proposal was "a disservice to the American public." While the Commission has been accused of many things over the years, somehow, I doubt individual and small business mailers feel disserved because the Commission chose to allow time for carefully evaluating the legal and economic ramifications of rules which could permit a few large volume mailers to cut deals directly with the Postmaster General for special, undoubtedly lower, rates.

Seriously, the commenters raised important concerns about the proposals we viewed as less controversial. For example:

> "If the Commission were to adopt its proposed rules, it would be faced with making its decisions on a one-sided record submitted by the Postal Service. Opposing parties would have no valid opportunity to make an alternate case. The result would be a Postal Rate Commission that could not possibly fulfill it statutory responsibilities." And,

> "Thus, any financial losses stemming from ill-advised or underpriced 'new' or 'provisional' services under rules such as those proposed in the Notice would shift from the users of these 'new' and 'competitive' services to monopoly mailers. This would constitute a cross-subsidy of such services by First Class mail, and, as such, would contravene the intent of Congress."

Even the Postal Service has expressed dissatisfaction with the Commission's version of the proposed rules, although for a very different reason than the above-quoted commenters. It wants even more flexibility than the proposed rules would allow.

So, we are continuing to consider the issues raised by this rulemaking and will be able to give them even more attention when the experimental small parcel case is completed, particularly now that the initial phase of the classification reform effort is in hand.

When I was here last year, I also expressed some concerns with the information and data used by the Postal Service to support requests filed with the Commission. During the recent classification reform case, the Postal Service provided a number of cost studies which, I am happy to say, were at least up to the standards of earlier Postal Service cost studies. However, I do want to bring to the Committee's attention two potential problems with the data and information the Commission and the parties normally use to evaluate Postal Service proposals.

The first concern is with the timeliness of regular Postal Service data reports. The Commission rules, developed in conjunction with the Postal Service, provide for the regular submission of basic cost and volume data. It has been my experience that the Postal Service does not always submit this information in a timely manner, and this can pose significant difficulties to parties and the Commission when a case is proceeding. As an example, the basic Cost and Revenue Analysis report for 1994 was not filed until May 22, 1995, almost two months after the Postal Service classification reform request was submitted to the Commission. In contrast, the 1993 ver-

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[1] On October 27, 1995, the Commission published proposed rules for conducting proceedings on Postal Service requests for market tests of new services, temporary establishment of provisional services, and minor changes in mail classification, all in 120 days or less. Rules that would allow proposed new services to break even financially over a multi-year period were also included. Other rules proposed by the Postal Service concerning "limited scope" rate cases, rate bands, and negotiated service agreements, were held in abeyance.

[2] 60 Fed. Reg. 54981 (October 27, 1995)

[3] Ibid.

sion of that report was filed in March 1994. Since parties must file their direct case within four months, a two month delay poses a serious hardship.

The other issue I want to raise is the Postal Service's increasing tendency to withhold information or data it claims has some commercial value. Many private businesses appear before the Commission and voluntarily disclose what is clearly proprietary information. The Postal Service is not a private enterprise, although it is expected to operate in a businesslike fashion. It seems to me that the Service should avoid withholding information as proprietary unless it is clearly evident that disclosure would be likely to have a significant harmful impact.

Early in the classification case, the Postal Service was asked to provide information on its customers' reaction to a reduced rate for courtesy reply mail. Initially, the Postal Service resisted providing any information. Then, when pressed, the Postal Service provided a relevant study with certain portions redacted. When the Commission insisted that the Service explain why this information was withheld as proprietary, it became clear that there was little or no likelihood that this information would have harmed any Postal Service business interests.

Unfortunately, the process for obtaining data not willingly provided by the Service can extend for months. Thus, by interposing meritless objections, the Postal Service withheld information sufficiently to reduce its value to participants in the case. A similar controversy delayed participant access to a report highly relevant to Postal Service claims that alternative delivery of second-class publications was an economic threat. As I noted when we issued our decision on January 26: "[t]he record evidence indicated that there was no real competitive threat in this area—a conclusion supported by a summary of a Postal Service study which became available through discovery. Interestingly, the Postal Service witness in this area was not apprised of the existence of the study while preparing his expert testimony."

I recognize that there may be some proprietary business information which the Postal Service might need to withhold. But as long as the Postal Service remains the nation's provider of monopoly mail service, it should be willing to operate in the sunshine and allow the American people to understand both its successes and its failures.

Partly because of these difficulties, I am reversing a position I took last year. You may recall, I was asked whether I thought the Commission should have statutory authority to subpoena Postal Service records and documents. I said I was not ready to ask for that power. Now I am, and as the Subcommittee proceeds to consider postal reform legislation, I urge you to give the Commission that authority.

The Commission believes there are other legislative changes which could benefit the ratesetting process. But that is not the subject of this hearing. We look forward to sharing our thoughts on this in the future, and, of course, we offer our services and assistance to the Subcommittee as it proceeds.

LETTER FROM TIMOTHY J. MAY

IN RESPONSE TO EDWARD GLEIMAN'S LETTER ADDRESSED TO SENATOR STEVENS

PATTON BOGGS, L.L.P.,
WASHINGTON, DC
March 29, 1996

The Honorable Ted Stevens, *Chairman*
Subcommittee on Post Office and Civil Service,
Committee on Governmental Affairs,
United States Senate,
Washington, DC.

DEAR MR. CHAIRMAN: I have been provided with a copy of a letter addressed to you by Edward Gleiman, the Chairman of the Postal Rate Commission, dated, March 18, 1996. This letter addresses a portion of the testimony given by me to your Subcommittee at its hearing on March 14, 1996. Chairman Gleiman's letter complains that my testimony which related to testimony he had given to the House Subcommittee on Postal Affairs concerning the courtesy envelope mail issue (CEM) was inaccurate. Chairman Gleiman states that his testimony regarding CEM was only a minor part of his testimony; that the Commission's proposal was not for a deeply discounted rate category; and alleges that I may believe it is inappropriate for him to respond to questions from a Congressional Subcommittee.

To begin with, my testimony made clear I had not heard Chairman Gleiman's testimony but that I was referring solely to the account of his testimony in *The Wash-*

ington Post. I am enclosing a copy of that article; as is evident, the article would lead one to believe that the principal subject of the Chairman's testimony was the CEM issue. I certainly have no question that it is appropriate for the Chairman of the Postal Rate Commission to respond to questions posed by Congressional panels. My objection was that the Chairman made what I believe are inappropriate comments for a quasi-judicial body when the Chairman charged the Postal Service with lying to the American people. To quote the headline of the article: "Agency Broke Promise, Rate Panel Chief Says."

As to the question of whether the CEM would call for a deep discount, Chairman Gleiman's claim that the Commission's recommendation was simply for a "shell" classification and called for no rate discount is disingenuous. Chairman Gleiman well knows that the adoption of this "shell" classification would require the Commission in the next rate proceeding to recommend a rate discount for that class, as deep a discount as it wished, with the Postal Service having no choice but to accept it or to lose their entire rate request. As my testimony to you made plain, the author of this proposal, the Consumer Advocate at the Postal Rate Commission, asked for a 12 cent discount; their lead expert witness furthermore testified that in order to pay for this discount there should be a 1 cent increase in all first class rates. It is obvious that the only reason the Commission did not recommend a discounted rate for the CEM "shell" was that they would not have been able to find the money to pay for it except through an increase in first class rates, which they would find politically unpalatable.

Chairman Gleiman also took issue with my testimony that the CEM rate would have as its principal beneficiary a few large companies who use Business Reply Mail. Chairman Gleiman states that: "If it were eligible for the CEM discount it would comprise a small percentage of mail in the CEM category." Apparently, the Chairman is unaware that the evidentiary record makes clear that the proposed CEM would include Business Reply Mail; moreover the Chairman is simply wrong as to what percentage of CEM would be in that category. It would comprise a significant percentage of the CEM category. Chairman Gleiman says, even if such mail were included, it would be appropriate because it is cheaper to handle. I do not question the fact that Business Reply Mail might be entitled to a discount because those who are paying the postage, that is, the companies who supply the Business Reply Envelopes to their customers, are the ones who are responsible for the savings, and it would be appropriate for them to be the beneficiaries of such a discount. On the other hand it seems entirely unfair to penalize the companies who provide the CEM envelopes to their customers (who do nothing to earn a discount) by making those companies pay higher postal rates to make up for the hundreds of millions of dollars of lost revenue from CEM discounts.

Finally, I certainly have no objection to debating these issues with Commissioners before a Congressional Committee; that is simply a revisitation of the very same arguments that were presented before that Commission. And certainly, the Commission should be perfectly free to explain its decisions to duly constituted Congressional bodies when they ask for such explanations. My fundamental objection to the testimony was that it went beyond the kind of judicial explanation one would expect and attacked another federal agency, accusing it, in effect, of lying to the American people. That is a distortion that undermines the confidence of the American people in one of its major institutions, and tends to politicize what should be a judicial process.

As always we appreciate the opportunity to present our views to the Congress and I would ask that, if Chairman Gleiman's letter concerning my testimony is included in the hearing record, this response to that letter also be included.

Sincerely yours,

TIMOTHY J. MAY

Enclosure

ARTICLE FROM THE WASHINGTON POST

AGENCY BROKE PROMISE, RATE PANEL CHIEF SAYS

BY BILL MCALLISTER

Washington Post Staff Writer

The chairman of the Postal Rate Commission yesterday accused the Postal Service of reneging on its promise to let individuals share in the savings from the agency's multibillion-dollar automation program.

Commission Chairman Edward J. Gleiman told a House subcommittee he was astonished by the refusal of the Postal Service Board of Governors to accept a proposal that would have allowed individuals to pay less than 32 cents a letter for paying bills in envelopes preprinted with address bar codes. Such envelopes are widely used by credit card companies, department stores, utilities and other firms that receive payments by mail.

Despite repeated suggestions that it was going to offer individuals a discount to encourage use of such mail, the Postal Service last week rejected a commission proposal to give such letters a yet-to-be-determined discount. The governors cited the potential loss of "hundreds of millions of dollars" in stamp revenue and operational problems from handling two types of stamps.

The rejection infuriated Gleiman. His small agency is fighting a Postal Service proposal to strip the commission of some of its powers to regulate postal prices. Yesterday, Gleiman used a joint hearing before the House Government Reform and Oversight subcommittee on the Postal Service to charge that the postal governors, presidential appointees who oversee the agency, "may have been misled by postal management" into rejecting the latest discount proposal.

Asked about Postmaster General Marvin T. Runyon's earlier suggestion that the discount proposal was unworkable, Gleiman countered: "Plain and simple, the postmaster general is wrong."

Gleiman last year upstaged Runyon by telling the subcommittee that the Postal Service had shunned a way of getting quicker decisions from his agency. This year he cited a 1995 news released as evidence of the agency's duplicity on the discount proposal. "The Postal Service plans to ask the Postal Rate Commission at a later date for a lower rate based on the lower costs of automating this mail," the release read. "These savings would be passed on to the consumer."

"When the Postal Service makes such a public commitment, should not the public be able to take the service at its word?" Gleiman asked. "Apparently not."

Asked to explain whether the agency had misled the public, postal spokesman Frank Brennan said after the hearing that the agency had not intended to create the impression that it would seek a separate rate for the reply envelopes. "It was not an artfully crafted paragraph," he said.

What the agency meant to suggest is that customers would benefit from "indirect savings" that result from the use of bar-coded envelopes. These envelopes help absorb the higher costs of processing handwritten envelopes and give customers a lower-priced first-class stamp for their mail, he said. Consumers benefit by "averaging" the two types of letters under the 32-cent rate, he said.

Although David Fineman, a newly appointed postal governor from Philadelphia, had suggested last week the governors might yet approve a discounted "citizens' stamp," Brennan indicated that the odds were against creation of such a separate stamp. "We have always felt that a separate stamp was a bad idea operationally," the spokesman said, adding that remains the agency's position.

He said postal officials fear "ill will" and other problems from the possible improper use of a discounted stamp. Besides, had the service accepted the commission's proposal for the stamp, it might be locked into a discount that it could not later accept, he said.

As early as 1988, the Postal Service had suggested that a discount stamp was "worth further consideration" and suggested it wanted to study the idea. At one time the rate commission had suggested a 2-cent letter discount and more recently the commission's consumer advocate had proposed a 12-cent discount. The rate commission did not set a specffic rate in its latest proposal, but said it would allow the Postal Service to return to the commission to set the rate in another proceeding.

Gleiman said there is abundant evidence that return letters with preprinted bar codes are cheaper than other letters to handle. Usually such letters are picked up at a post office and don't have to be delivered. Because they have preprinted address bar codes, they can be sorted by machines, he noted.

The dispute over discounted letters illustrated that, despite improved working relationships between postal officials and the rate commission, tensions between the two agencies remain high. Gleiman, a former Senate staff member, also used the hearing to under-cut another Runyon argument that the commission takes too long—up to 10 months—to consider major rate increases.

As Runyon and Tirso del Junco, chairman of the governors, left the witness table, Gleiman presented them with copies of a commission decision approving an experiment that will give discounts of 4 cents a parcel to first-class packages and Priority Mail envelopes that come to test post offices in three locations.

The agency had asked for a expedited ruling in 120 days. The decision was issued in 85 days and was only the second time the Postal Service had asked for expedited decision-making, Gleiman said.

In his testimony, Runyon continued to paint a bleak picture of the agency's declining mail volume, but he did announce that the agency's two largest unions, the American Postal Workers Union and the National Association of Letter Carriers, have agreed to his request for a labor summit.

The yet-to-be-scheduled meeting will feature discussions on ways to end the agency's acrimonious labor relations.

RESPONSES TO QUESTIONS FROM SENATOR STEVENS BY JONAH GITLITZ

DIRECT MARKETING ASSOCIATION, INC.
WASHINGTON, DC.
April 5, 1996

The Honorable Ted Stevens
U.S. Senate
Washington, DC.

DEAR SENATOR STEVENS: It was an honor to be asked to participate in your Subcommittee Hearings on Postal Service Modernization—the Customers' Prospective. I have enclosed my responses to your written questions which follow-up my prepared and oral remarks at the hearing.

On behalf of all the members of the Direct Marketing Association and its Board of Directors, I greatly appreciate your interest in maintaining a strong, financially viable and universal Postal Service. The Postal Service is a vital link between direct marketers and their customers throughout the U.S.

I look forward to working with you, your Subcommittee and your staff on postal reform legislation. If DMA can assist you in this effort, please feel free to call upon us.

Sincerely,

JONAH GITLITZ

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1. Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

A. At this point, DMA is not sure whether or not the Postal Service should be free to set rates for non-monopoly services. DMA's draft legislation regarding postal reform (attached to my prepared testimony) does not include any such provision, precisely because of your concern—the difficulty and contention in drafting safeguards for the monopoly classes. However, if the Postal Service were to set rates for non-monopoly services, then DMA offers several solutions to the problem of forced cross-subsidization. While these solutions are very feasible, the details of these solutions require more study and careful drafting.

One important solution to prevent cross-subsidization is to require all services, including non-monopoly services, to cover their attributable costs as determined in the most recent omnibus rate case. By doing so, you create a floor for the rates of non-monopoly services, freeing the Postal Service to set rates anywhere at or above that floor. Inherent in this solution is the idea that if the non-monopoly services lose money, then their rates—not the monopoly services—must recover the losses.

Another possibility to the dilemma of cross-subsidization is to create a separate subsidiary of the Postal Service which would provide for non-monopoly services. This subsidiary would not and must not operate at a loss, therefore preventing any cross-subsidization from the monopoly services (First- and addressed third-class mail).

2. It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?

A. DMA's testimony agrees with the other witnesses on this issue. As long as the Postal Service has a statutory monopoly over any service, there must be some regulatory body overseeing the pricing of that monopoly service.

However, DMA does not take issue with the structure of the Postal Rate Commission in its call for reform. The role, authority and charge of the Postal Rate Commission is what DMA has called into question. DMA believes that the Postal Service, even as a monopoly, must be given some pric-

ing flexibility so that it may survive into the next century. At the same time, as a monopoly, the Postal Service should not be given *carte blanche* pricing authority. With this parameter in mind, the Postal Rate Commission would then have an auditing role in any pricing flexibility granted to the Postal Service. In addition, DMA believes that, in granting flexibility, the Postal Rate Commission should also be charged with examining the cost and rate relationships among all Postal Service offerings through rate change requests that are filed by the Postal Service after a set number of years (5 years in DMA's draft).

DMA would also like to see the Postal Rate Commission granted subpoena power. One of the major complaints that both the Commission and mailers have raised in rate cases is that the Postal Service is either slow or unwilling to provide adequate data so that rates may be accurately set. DMA believes that giving subpoena power to the Commission would help to eliminate this problem and allow the Commission to move quickly in their deliberations.

Several witnesses have suggested that there be specific qualifications for a candidate to be considered for the Postal Rate Commission and that the nominees be rated by an economic or legal professional association. DMA does not oppose these suggestions of specific qualifications for members of the Postal Rate Commission.

3. All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?

A. Very simply, they won't. As the testimony of Chris McCormick, Senior Vice President, L.L.Bean, vividly illustrates, mailers are constantly looking for new ways to control costs—postage costs—and still meet the needs of their customers. The new media are now offering new opportunities for mailers, and the Postal Service must be able to respond to those new opportunities if it is to survive as we know it. Postal Service volume has already been affected in five of six markets. If we want to maintain universal service, the Postal Service must become more competitive to keep and expand mail volume. Significant erosion in volume will mean skyrocketing rates for all mail users, including First-Class. As Mr. McCormick testified, L.L.Bean has already shifted $45 million of postage costs to other media and competitors of the Postal Service. L.L.Bean is not alone. As mail volume moves elsewhere, out of the Postal Service, the mail that remains in the system must pick up a greater and greater share of the network costs of the Postal Service. This will cause rates to rise further and increase the pressure on mailers to leave the system. This downward spiral makes it difficult to imagine a universal delivery Postal Service surviving without taxpayer assistance—a full circle back to 1970.

4. I am intrigued by the outline of your draft legislative package. Many of these ideas have been floating around for a while but it appears that DMA has provided a little more meat on the bones.

Under your proposal, there would be an omnibus rate case at least every five years and between rate cases the Postal Service could raise rates by up to 75 percent of the consumer price index. I noted, however, that under your proposal all rates would be changed by the same proportion.

Does this mean that the Postal Service would be required to raise all rates by the same proportion at the same time?

A. Exactly. The Postal Service, using its rate indexing authority, would be required to raise all rates by the same proportion at the same time. If the Postal Service wanted to raise rates in different proportions, it would be required to use the current ratemaking process (filing a rate change request with the Postal Rate Commission).

I must add that DMA's proposal does not *require* an omnibus rate case every five years. The Postal Service may not change its rates using its indexing authority more than five years after an omnibus rate case; however, the Service would be able to delay a rate request at the Postal Rate Commission well beyond five years.

5. What is the rationale for allowing the Postmaster General and the Deputy Postmaster General vote on all Postal Rate Commission recommendations?

A. DMA believes that the Postal Service must be held accountable for its performance. The Postmaster General and the Deputy Postmaster General are responsible for directing the performance of the Postal Service and, thus, must be held accountable for it. Since Postal Rate Commission recommendations significantly affect any actions the PMG and DPMG take in directing the Postal Service, they should be able to fully participate in any decision to accept, reject, allow under protest or modify those recommendations.

6. You surprised me by including subpoena power for the Postal Rate Commission for information related to rate and mail classification case issues. Do you envision that the information received from the Postal Service under subpoena would then be made available to all participants in the rate or classification case?

A. Even with subpoena authority, the Postal Rate Commission would be required to render its recommendations based upon a *public* record. Thus, all information received by the Postal Rate Commission through a subpoena would be placed on the public record. Of course, if the Postal Rate Commission requested privileged information, the Postal Service could seek to quash the subpoena or, as is currently done with some privileged information given to the Postal Rate Commission, the Postal Service could request protective conditions on certain data which would be given to all parties under strict use guidelines. In any event, all parties would have use of any subpoenaed information.

RESPONSE OF IAN D. VOLNER ON BEHALF OF AMMA TO SUBCOMMITTEE FOLLOW-UP QUESTIONS FROM SENATOR STEVENS

VENABLE, BAETJER, HOWARD & CIVILETTI, LLP
WASHINGTON, DC.
April 10, 1996

Ms. Pat Raymond, *Staff Director*
Post Office and Civil Service Subcommittee
Room 601, Senate Hart Office Building
U.S. Senate
Washington, DC

Re: *Follow-Up Questions to March 14 Postal Hearings*

DEAR PAT: I am enclosing my responses to the further questions put to me, in my capacity as general counsel to AMMA, as the result of the testimony we presented at the Subcommittee Hearing on March 14, 1996. To facilitate their inclusion the record, each question is stated verbatim, followed by the response.

I thought the questions were extremely thoughtful and incisive and I am hopeful that my answers will further the efforts to modernize the Postal Reorganization Act. If we can be of further assistance on this matter, please do not hesitate to call on me.

Sincerely,

IAN D. VOLNER

cc: The Honorable Ted Stevens

RESPONSES TO QUESTIONS

Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

The Advertising Mail Marketing Association believes that the solution to rate regulation of "non-monopoly services" lies in benchmark regulation, under which the Postal Service would be allowed to adjust rates for all services—monopoly and non-monopoly alike—with minimal regulatory review, so long as the adjustments fall within clearly defined objective parameters. Under benchmark rate regulation, the floor on all rates would be attributable or direct cost. The increase for any subclass, including non-monopoly subclasses, would be established by reference to the consumer price index. There are two difficulties associated with complete deregulation of so-call non-monopoly services. First, it is very difficult to define which services should be treated as "non-monopoly". There are several subclasses of mail which are legally exempt from the Private Express Statutes but as to

which the Postal Service faces little or no competition. Secondly, as the Subcommittee's question correctly observes, there is the danger that the Postal Service will subsidize its rate for non-monopoly services through rates charged to the monopoly classes. The benchmark approach avoids these problems, by assuring that there are no intersubclass subsidies while at the same time enabling the Postal Service to offer competitive rates for those services in which it faces competition so long as it is able to control its costs.

It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?

We regard questions about the structure of the Postal Rate Commission as premature. The central problem with the Commission is not related to its structure but its adherence to rate making criteria that fail adequately to reflect the competitive environment in which the Postal Service now operates. Changing those criteria for omnibus rate cases, and through the introduction of benchmark regulation and the authorization of negotiated service arrangements may, over time, warrant reexamination of the role of the Rate Commission. But that question ought not to be addressed until we have garnered sufficient experience under a modernized Postal Reorganization Act to meaningfully understand what sort of changes are then appropriate.

All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?

It is exactly this concern that underlies AMMA's call for modernization of the Postal Reorganization Act. If the Postal Service is to maintain and improve the universal service it now offers to all Americans, it must be provided with incentives and the tools to operate in a competitive environment. Experience has taught us that taxpayer subsidies to support the Postal Services basic public service functions do not work, and they have all been phased out. It is our belief that the Postal can maintain universal service at reasonable prices if it becomes market-driven, efficient and responsive to the needs of its customers; AMMA is convinced that the ratemaking standards and the barriers to creative and co-operative labor relations of the 1970 statute must change if taxpayer subsidization of the postal system is to be avoided.

I am intrigued by your suggestion that the Postal Service should be allowed to price services based upon a benchmark. I also noted that you specifically recommend that rates should not be set below direct costs. Do you envision that the Postal Service could set rates which do not include institutional or overhead costs, or do you include those costs when determining the floor?

Under benchmark rate regulation, as we envision it, "direct cost" or attributable cost would represent the floor on rates for all classes and subclasses of mail; that floor does not include any allocation of institutional cost. Of course, in order to institute benchmark rate regulation, baseline rates for all classes and subclasses would have to be established and those baseline rates would have to include institutional cost to assure that the Postal Service achieves break-even. On a going forward basis, however, rate adjustment would be measured solely on the basis of the CPI so long as the Postal Service is able to control its cost. There are several reasons for excluding institutional costs from the rate floor on a going forward basis, the principal one of which is that allocation of institutional cost primarily involves marketing decisions that are best left to the Postal Service. So long as all classes cover attributable costs and do not experience increases disproportionate to the rate of inflation, no mailer and no competitor of the Postal Service is harmed by the Postal Service's marketing judgments. If, however, the Postal Service cannot control its costs under the benchmark rules we have proposed, it would be required to file an omnibus rate case in which institutional cost coverages might be adjusted.

You suggested that surpluses earned under the benchmark rate should be shared with all employees, so long as certain financial and performance goals are met.

Would you expect that the mailers would share as well? Maybe in the form of stable rates or even a rate decrease?

Mailers certainly would benefit from surpluses earned by the Postal Service under a benchmark rate system in several ways. Benchmark rate making would provide the Postal Service with powerful incentives to earn surpluses. Although we anticipate that some portion of surpluses will be shared with all employees, we also assume that some portion of the surpluses will be applied to reduce the Postal Services outstanding indebtedness or to forestall the need for additional borrowing. Reduction in interest costs should further enable the Postal Service to stabilize rates (foregoing benchmark increases) and possibly to affirmatively reduce them.

You specifically recommend that Congress establish new ground rules for outsourcing at the Postal Service which define the circumstances in which the Postal Service is permitted to contract out. I was particularly intrigued with the follow-on suggestion that the Postal Unions be allowed to bid as well. Do you have any comments on some of the specific circumstances which you believe should be included in such guidelines?

In AMMA's view, guidelines for defining the circumstances in which the Postal Service is permitted to contract out is a question best addressed by the Postal Service and its unions. Basically, however, our view is that the Postal Service should be permitted to contract out (or out-source) any functions related to the acceptance, processing or delivery of mail so long as (a) the Governors are provided with evidence establishing a basis for concluding that the function can be performed more cheaply in the private sector, (b) the proposal is put out for bids, (c) any bargaining unit or operating unit of a postal union may bid for the work and (d) the Governors approve the final contract on grounds that it will, in fact, result in measurable cost savings to the Postal Service. As we envision it, these out-sourced functions need not and probably would not be national in scope but would, for the most part, involve localized activities. We note that the Postal Service now contracts out with rural carrier delivery and certain small post offices.

LETTER FROM CHRISTOPHER J. MCCORMICK TO SENATOR STEVENS

L.L.BEAN,
FREEPORT, MAINE
March 26, 1996

The Honorable Ted Stevens, *Chairman,*
Senate Committee on Governmental Affairs
United States Senate
Washington, DC.

DEAR SENATOR STEVENS: It was both an honor and a pleasure to have the opportunity to appear before the Senate Committee on Governmental Affairs to share L.L.Bean's concerns and perspectives on matters related to the United States Postal Service. I hope that I was able to convey my Company's continuing commitment to the Postal Service, but also our growing concern that reform is necessary to ensure the Postal Service's continued economic viability in the face of increasingly significant competitive pressures.

Enclosed please find our responses to the questions you sent on March 15th. I have tried to keep our responses brief and to the point of the questions. If you or your staff have further questions, we would be happy to respond. I have also taken the liberty of enclosing a copy of L.L.Bean's corporate position on Postal Service Goals and Objectives.

Again, on behalf of L.L.Bean, I am delighted that you are focusing your efforts on the U.S. Postal Service, and reiterate our commitment to assist you and your Subcommittee in any way that we can.

Sincerely,

CHRISTOPHER J. MCCORMICK

Enclosures

RESPONSES TO QUESTIONS

1. Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

This is a very difficult question to answer in the abstract. The ability to set rates for non-monopoly services invites a number of fair trade issues, each of which needs to be addressed by countervailing regulatory mechanisms. Included among the problems that can arise are:

- The temptation to assign costs against monopoly services where the certainty of recovery is far greater through the regulatory process than it may be through the competitive market.
- The ability to use the monopoly services to cross-subsidize pricing structures for non-monopoly services and thereby disadvantage competitors in those markets.
- The potential for "tying" the use of monopoly services to the use of non-monopoly services.
- The opportunity to use the size and market position of the monopoly component of the enterprise to attract capital and other resources that will be used in the non-monopoly segment of the enterprise on more favorable terms and conditions than competitors. This would disadvantage competitors in these markets, and may also result in increases in the riskiness of the monopoly component and a corresponding increase in the cost of capital.

Having identified these concerns, it is important to stress that they are not unique to the USPS, but are rather endemic to any industry undergoing partial deregulation. For example, the telecommunications industry, the electric utility industry and to a lesser extent various components of the transportation industry have each seen their "natural monopoly" positions eroded through changes in technology or consumer demand in certain aspects of their business, e.g., long distance service, yellow pages, etc. In each case, the result has been the development of new regulatory structures that permit competitive entry and limited deregulation of the incumbent provider in these market segments. We would suggest that the models developed for the railroad industry (Interstate Commerce Commission), the telecommunications industry (Federal Communications Commission and various state Public Utility Commissions) should be examined very carefully as they appear to have substantial applicability to the U.S. Postal Service. For example, many State Public Utility Commissions have initiated "performance-based" or "incentive" regulation systems in lieu of traditional rate of return regulation to regulate the dominant providers of local telephone services in their state. These systems are structured to minimize the risks of cross-subsidization by establishing rates based on a set of generic principles described below:

- Services provided by the utility are divided into those that are subject to effective competition in the marketplace, i.e., they are not "natural monopolies", and those that are essential services and remain effective monopolies.
- For those essential services that remain effective monopolies, the pricing decisions of the utility continue to be regulated by the Public Utilities Commission, often through the development of specific pricing indices or other such pricing formulas. As a general rule, these formulas permit a utility to change prices based on the difference between inflation and a productivity offset. They are designed to minimize regulatory oversight, while protecting ratepayers from unreasonable price increases and ensuring that ratepayers share a portion of the benefits of technological innovation and increased productivity. (For the Postal Service, it would seem to make more sense to establish a single multi-year rate to avoid the expense associated with annual rate changes.)
- The prices for those services subject to effective competition are left to the discretion of the utility, within certain boundaries established by the Public Utilities Commission. Generally, the utility is not permitted to price these services below long-run incremental cost to ensure that it does not use its monopoly position to cross-subsidize this set of services to the detriment of potential competitors in the market. Until there is viable competition for catalog delivery, customers like L.L.Bean would require some form of rate protection to guard against unreasonable rate increases due to lack of alternatives. One possibility would be to require the PRC to recommend a minimum and maximum rate for each competitive service.

- There usually exist certain safety valves in these types of regulatory structures which permit the utility to share the burdens of unforeseen and exogenous costs with ratepayers as well as pass on a portion of the benefits of unforeseen events to its ratepayers.
- Under these types of regulatory systems, the utility is generally permitted to enter into special contracts with certain customers for the provision of monopoly services at negotiated rates. These contracts are specifically at the risk of the utility, and thus any foregone revenues are borne by shareholders, even though it may be argued that all ratepayers benefit by keeping these customers "on the system" albeit at lower levels of contribution to the utility's overhead costs.

In addition, there are provisions that cover the entry of the utility into new lines of business, including the establishment of unregulated subsidiaries. These are designed to ensure that transactions between the regulated utility and its unregulated subsidiaries are conducted at "arms length" and that the full costs of the subsidiary are reflected in its pricing structures.

2. It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?

L.L.Bean is not sufficiently versed in the structure of the Postal Rate Commission to comment on specific changes that should be made. We would defer to our trade associations—the Direct Marketing Association, the AMMA, etc.—which represent us and other members of our industry before the Postal Rate Commission and are thus more knowledgeable about he Commission's operations and shortcomings.

There are three issues, however, that we would like to highlight as candidates for reform. First, we believe that voting membership on the Board of Governors should be extended to both the Postmaster General and the Assistant Postmaster General. (Neither, however, should be permitted to hold the position of Chair of the Board of Governors.) This is consistent with the policies of the overwhelming majority of publicly-held corporations, wherein the highest officers of the corporation are members of the Board of Directors. At the same time, it does not jeopardize the position of the Board as an "outside" directorate.

Second, we believe that the Board of Governors should be able to override actions of the Postal Rate Commission with a two-thirds vote majority, rather than the unanimous vote now required. This change would give the Board of Governors more authority and ability to respond more quickly to critical issues faced by the Postal Service.
Finally, we recommend that the nomination and selection process for the Postal Rate Commission be restructured. In particular, we suggest that this process be modeled on the process used by many governors to develop nominations for judgeships and other quasi-judicial positions, e.g., Public Utility Commissions, Workers Compensation Boards. In these instances, a nominating panel from a professional organization, such as the State Bar Association, is charged with developing a list of nominees. The governor is at liberty to choose from among the nominees presented, and the nominee is then subject to legislative confirmation. While the qualifications for Postal Rate Commission membership are more varied then for the judicial system, for example, and thus the pool of potential nominees substantially broader, we believe it is nevertheless possible to construct a nominating process that emphasizes the professional qualifications and skill levels of potential nominees, as evaluated by peers in their respective fields.

3. All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?

We do not believe that the Postal Service will be able to sustain its basic service function without taxpayer support if it is unable to maintain its market share in its traditional markets as well as capture market share in new communications markets. Thus, we believe very strongly that it is important to provide the Postal Service with the wherewithal and the incentives to compete more effectively in what it currently does and seek new opportunities in such areas as electronic communications and higher value-

added markets where higher margins are possible and commensurate with higher service standards.

4. I noted that one of your business decisions was to discontinue using the Postal Service to deliver your packages and move to private sector alternatives. Under what circumstances would you be able to return your business to the Postal Service?

The decision to switch to UPS and then FEDEX from the USPS for our package delivery was based simply on price and performance, and our expectations about how effectively the different vendors would meet our needs in the future. Accordingly, there are three factors that we would examine very carefully prior to switching back to the USPS for package delivery:

- USPS pricing would have to fall to meet the competitive alternatives. This could be accomplished through a general reduction in tariffed rates or through a special contract rate developed for service between the USPS and L.L.Bean. Under the latter option, L.L.Bean would be willing to commit minimum volume utilization under a multi-year contract if the pricing is attractive.
- USPS service quality would have to improve. L.L.Bean would be unwilling to switch to the USPS unless the Postal Service was willing to commit to certain measurable performance standards that would apply at a minimum to our shipments. This commitment should be tied to financial consequences—penalties if standards are not met and rewards if they are met or exceeded.
- While L.L.Bean would look favorably on the kinds of changes noted above, we would also evaluate whether or not the management and regulatory structures that govern Postal Service operations were modified as well to accommodate these changes. To the extent that the current regulatory structure remains such that special contracts or performance standards and/or incentives are not encouraged, L.L.Bean would be less likely to change its package delivery vendor relationships to the Postal Service.

L.L.Bean's Position—Postal Service Goals and Objectives

L.L.Bean has a vital interest in the future of the U.S. Postal Service. The Postal Service is the largest supplier of goods and services to L.L.Bean with last year's volume surpassing $35 million, largely due to the mailing of over 140 million catalogs to American households. It's clear that L.L.Bean would not exist as it does today without a viable and productive Postal Service. Therefore, it is with great interest that L.L.Bean participates in the privatization debate and re-engineering process.

We are encouraged by the course Postmaster General Runyon has taken the past three years in stabilizing rates and support his efforts in reducing the regulatory and operating burdens under which the Service must compete today. We believe reforms must be implemented which are designed to promote innovation and instill a new level of cost-consciousness and market responsiveness in the Postal Service.

To better position the Postal Service to compete in the future, there are four, overriding goals that we seek in this process.

- Since the Postal System is the primary means of interface between our Company and our customers, we require service that is timely, reliable, and consist. Service performance standards must be established, measured and publicly reported.
- Our business is a highly competitive one and where- the marketplace consistently disciplines higher cost suppliers. At a minimum, we require rate stability and believe that rate reductions are reasonable given the rate increases experienced over the past decade. Investments in innovative technology and automation should continue to mitigate anticipated cost increases.
- L.L.Bean services a national and increasingly international customer base. Accordingly, we require a postal service which provides access to all households/addresses in the country and serves as a gateway to international markets.
- Our marketplace is also a very dynamic one where technology and consumer expectations are combining to redefine the relationships between ourselves and our customers. It is imperative that the Postal Service keep abreast of technological developments across the full communications spectrum. Through the development of culture of innovation and ex-

cellence within the Postal Service, we expect our Company will be provided with access to innovative services and new products in a timely and cost effective manner so that we are able to compete effectively and to serve our customers better.

It is L.L.Bean's hope that the adoption and attainment of these goals by the Postal Service will permit us to supplement, and not supplant, our traditional means of communicating with our customers. And, in the process, we would like to become an even larger customer of a more efficient and more effective Postal Service.

Once the necessary reforms are in place, we believe the Postal Service should be free to improve its internal operating structure to promote productivity and granted more decision making authority in the establishment of postal rates and introduction of new services. The intent of the reforms should be to ensure that both the internal and external rules and systems governing Postal Service operations are designed to permit the organization to function as a business and to compete effectively for its customers.

In this new environment, the Postal Service should be held accountable for service quality and efficiency, as well as other performance standards agreed to by the Service's stakeholders.

We recommend a five year review process to determine the success of this reform. This requires that clear objectives and measurable performance standards are established and publicly reported. If service quality and efficiency have improved, additional reforms may not be needed. If not successful, other alternatives, such as moving towards competition, may warrant consideration.

Since 1912, L.L.Bean has enjoyed its partnership with the USPS. We make every effort to establish strong working partnerships with our key suppliers. These partnerships are more than simple contractual relationships. They involve commitment and substantial investment from both parties and are based on mutual trust and achieved performance. L.L.Bean would very much like to count the Postal Service among its most valued partners and is willing to extend its full commitment in working toward that objective over the next 5 years.

LETTER FROM CARY H. BAER TO SENATOR STEVENS WITH RESPONSES TO QUESTIONS

READER'S DIGEST ASSOCIATION, INC.,
PLEASANTVILLE, NY
March 26, 1996

The Honorable Ted Stevens
Hart Senate Office Building
Washington, DC.

DEAR SENATOR STEVENS: Thank you for permitting me to participate in your Subcommittee Hearings on USPS Modernization. You have asked me to respond to questions that could help in the drafting of legislation. Here are your questions and my responses:

1. Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

As stated in my testimony, I believe the Postal Service should be allowed to set rates in the non-monopoly classes. The Postal Rate Commission should act in an audit capacity to review postal rates and costs to ensure that there is no cross subsidization between classes of mail.

2. It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized postal service. What specific changes would you make to the current structure?

As I indicated in my testimony, my initial change would be to take away from the Postal Rate Commission the responsibilities for rate setting in the non-monopoly classes. However, I would empower the Postal Rate Commission to define and then determine monopoly and non-monopoly classes. I would not recommend any other changes to the Postal Rate Commission's authority/responsibility at this time, but would wait to see how these recommended changes work.

3. All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace,

how will they be able to continue the basic public service function without taxpayer support?

The answer to this question is simple. Without tools and flexibility in this competitive market, the Postal Service will not have the ability to continue without taxpayer support.

4. I noted your comparison of electronic banking and electronic bill payment capability to the growth curve of the fax. I think you are absolutely correct that this will have a major impact on the Postal Service. From your perspective, is there any way that the Postal Service could, or should become a player in this market?

Some have suggested that the Postal Service, because of its unique relationship as a trusted public servant, take on certain functions to guarantee security over electronic communications. Other than being given legislative authority to enter into a venture like this (security over communications), I do not believe that the Unites States Postal Service should be given any special consideration in the electronic marketplace.

5. I noted your suggestion that the Postal Service be given pricing freedom and flexibility on two specific non-monopoly categories: Parcel Post and Express Mail. As you know, parcel post is very important in Alaska. If the Postal Service were to be granted this authority, how would you expect that the parcel post rates in a rural state like Alaska would be impacted?

I have recommended in response to question 1. that the Postal Rate Commission be given the responsibility to determine whether a non-monopoly situation exists. It is entirely possible that Alaska is a special situation and that the United States Postal Service has monopoly status there for parcel deliveries. If that be the case, the USPS would not be given pricing flexibility in Alaska.

6. You and others have recommended that Postal Service and Management find some way to get along. As you know, it is impossible to legislate cooperation. You have recommended that there be a meaningful productivity and profit sharing system established. Should this be done through a cooperative agreement between the Postal Service and all of its unions, or do you recommend that Congress devise and mandate such a system?

Union and management relationships can be the most difficult in business. I would not recommend that Congress devise and mandate the relationship between the Postal Service and its Unions. However, perhaps through legislative oversight hearings, the Congress can utilize a "bully pulpit" to let both sides know how important a productive and cooperative environment between the Postal Service and its Unions is to their *mutual success.*

I trust these responses will be helpful to your Subcommittee in drafting USPS modernization legislation. I will look forward to answering any other questions that you or the Subcommittee have on this subject.

Best regards,

CARY H. BAER

QUESTIONS AND ANSWERS FROM THREE GREETING CARD COMPANIES

GREETING CARD ASSOCIATION
March 25, 1996

The Honorable Ted Stevens, *Chairman*
Senate Subcommittee on Post Office and Civil Service
Washington, DC.

DEAR SENATOR STEVENS: Enclosed are the responses to your questions regarding Postal reform from the following members of the Greeting Card Association:

Hamilton Davison, GCA President
Jack Mayer, Chairman of the GCA Postal Affairs Committee
Jeff Weiss, GCA Vice President

Thank you for allowing us to participate in the hearings and to respond to these additional questions. Please don't hesitate to call on us if we can be of help.

Sincerely,

MARIANNE MCDERMOTT
Executive Vice President

RESPONSES TO QUESTIONS FROM C. HAMILTON DAVISON, JR.

PARAMOUNT CARDS, INC.,
PAWTUCKET, RHODE ISLAND
March 22, 1996

The Honorable Ted Stevens, *Chairman*
Senate Subcommittee on Post Office and Civil Service
Washington, DC.

DEAR SENATOR STEVENS: Thank you for the opportunity to provide input to the legislative process concerning the Postal Service. I am impressed with the thoroughness of the Committee's investigations and the consideration with which the issues are being addressed.

To respond to the follow up questions raised in your letter of March 15:

- *Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?*

  No, the Postal Service should not be free to set rates for non-monopoly services. It is not that we are against this freedom per se; we cannot envision any way to provide this freedom while protecting the monopoly services from cross-subsidization.

- *It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized postal service. What specific changes would you make to the current structure?*

  I have no specific changes to suggest in the current structure of the PRC. I would provide the PRC with full discovery powers so they might make a fully informed inquiry into postal economics and the pricing decisions proposed to them.

- *You and Mr. Weiss both acknowledge that the Postal Service faces the same challenges as businesses—technology, competition, and changing consumer behavior. Further, you recommend that the Postal Service, as any other business, must reshape and revitalize itself to operate efficiently.*

  Do you have any specific suggestions about how the postal service can reshape itself to meet the competition aspect of this equation?

  Postal Service does need to compete in the marketplace into the next century. The Postal Service needs increased productivity incentives, management flexibility, automation and computer based systems.

  Control over the cost structure is critical. It may well be that unit volume of mail will decline due to electronic communications and other factors. It then becomes an inescapable reality that the USPS must down-size its work force to lower its overhead. How this is done is a political question. In private enterprise, under emergent conditions, we lay off employees. Under more planned circumstances, we attempt to use attrition, re-training and re-deployment for head count reduction.

- *What about the changing consumer behavior as it relates to greater use of alternative communications technology?*

  We believe that consumers will continue to use hard copy even as they increase their use of electronic communications. There are certain advantages a greeting card has over electronically transmitted or computer generated cards. To simplify, there are two schools of thought in our business about the future. One posits that paper based communication will go the way of the buggy whip. The other suggests that in an increasingly high tech world, the soft touch vestiges of our humanity will become even more important. At one time people believed the telephone would depress card usage. This certainly proved not to be the case as unit volume in our business continues to grow.

The total number of interpersonal communications is likely to rise as convenience goes up and cost goes down. This is why it is so important that we maintain a competitive cost structure in our national envelope delivery system; that we insure the system is reliable, easy to use, and timely; that we do not enact policies or regulations that say to our citizens: "we do not want your business" unless you mail in quantity or prepare your communications a certain way which may be beyond the capabilities of many households. Clearly, cost and features do impact consumer behavior.

The greeting card industry can and will do more to teach the value of written communication and can encourage cards and letters. This is an area we are just beginning to address.

- *You and Mr. Mayer are absolutely right that changes must be made to deal with the labor/management problems within the postal service. Do either of you have any specific ideas or models which we should consider?*

In the private sector, these issues are usually best left to top management. It may be that a solution in the public sector will require legislative encouragement. Congress may need to take the bold step to recognize that changes will be required, and at the same time it should set the ground rules under which such changes must occur.

I recognize that this is a complex and emotional area. As mentioned above, the courage to face the realities of the situation may be the best place to start. There should be explicit recognition that the total number of jobs in the USPS may need to decrease. Ideally, downsizing, if warranted, should come from attrition. Current employees should be placed in new jobs or retrained for new skilled areas. The real issue is productivity improvement and increased through-put. To improve productivity, job security for current employees (rank and file, and management) who are performing well may need to be established. People not meeting minimum performance expectations should be dealt with. In a union environment, gain sharing may be a strong incentive.

There are lots of models for success and failure in the world of business. I do not know how these must be modified to be applicable to the governmental or quasi-governmental environment of the USPS. I am not a labor-management expert. This notwithstanding, certain basic human needs and emotions are transferable in most environments.

At my company, we reduced headcount from 425 to 325 over an 18 month period on flat unit volume. We did this due largely to employee-led suggestions for improving productivity, simplifying processes, removing steps, improving the first pass yield and other ways to improve quality, reduce cost or shorten lead-time. We did not lay off a single person.

Quality initiatives have gotten a bad name in some circles as some managers have abused the process or failed to include the essential elements that secure the buy-in and participation of the worker. It's like ham and eggs: the chicken is involved but the pig is committed. Both management and worker need to be personally committed. Without real commitment to making it work, it surely won't. More, the secret of worker participation is management participation with the worker. It is the worker who controls the rate of implementation of any quality improvement.

How my company accomplished this, and put together a high performance culture, is a long and rather complicated story. Based on my experience, some of the essential elements include creating real employee ownership, creating a safe environment where people are willing to take risks, worker involvement in the improvement process, a carefully managed track record of success (pick the right lead-off projects), trust, communications, planning, and a long term commitment. Real improvements take years of concerted efforts. The implementation is the hardest part of the process.

- *All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?*

If revenue cannot be increased, then the costs must be decreased or taxpayer support will be necessary. While I have not made a full study of it, I am inclined to believe that it is possible to shrink the cost structure by

a very large percentage and still provide the basic public service functions Americans require from their Postal Service.

- *I noted in your testimony that your predecessor association was involved in the sending of V-Mail greeting cards during World War II. It has always been my notion that the Postal Service could take advantage of technology and offer a similar service—electronically transmitting a message which would be printed and delivered at the other end. In your opinion, would this be an appropriate function for the United States Postal Service?*

Naturally we believe that written communication between individuals is very personal and should be done in the traditional manner. At the same time, mass communication may well be amenable to some process utilizing electronics. This would seem to be a reasonable extension for the Postal Service since it utilizes one of the Postal Service's distinctive competencies, namely hard copy delivery. For instance, one could envision a tax form electronically stored and printed locally to reduce the cost of transport. Any improvement which leverages technology in the service of its core business and the one for which it has been given a protected monopoly is good. However, both for philosophical reasons, as well as self serving ones, we shun any proposal that includes the USPS competing with private enterprise. This is especially true if they compete with private enterprise using publicly built infrastructure or where the general public must bear the risk of such ventures.

Thank you again for your consideration. Let me know if I can provide further clarification.

Sincerely,

HAMILTON DAVISON

RESPONSE TO QUESTIONS FROM JACK B. MAYER

HALMARK CARDS, INC.
KANSAS CITY, MISSOURI
March 21, 1996

The Honorable Ted Stevens, *Chairman,*
Senate Subcommittee on Post Office and Civil Service
Washington, DC.

DEAR SENATOR STEVENS: I appreciate the opportunity to respond to your questions on Postal reform. I am impressed by the Committee's participatory process and the attention being given to these very complex issues.

- *Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?*

No, the Postal Service should not be free to set rates for non-monopoly services, because there would be no protection from forced cross-subsidization. If the Postal Service is able to reduce its costs through productivity improvements, etc., then it should be able to set more competitive rates while maintaining or increasing contribution to institutional costs, thereby avoiding cross-subsidization.

- *It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?*

We recommend that the current structure of the PRC not be changed. We believe that the PRC needs to have full discovery power for information needed in rate and classification cases.

- *All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?*

The Postal Service has a number of tools to compete in the marketplace. These include computer based systems, bar coding, automation, etc. The tool the Postal Service lacks to optimize its potential is the ability to rearrange its work force. This is a complex, challenging topic, but the objective of all parties should be the appropriate size and mix of skills to provide service efficiently and economically. The work force issue needs explicit rec-

ognition and action on the part of Congress and all constituencies. It may mean a smaller work force (or it may not, depending upon costs and unit growth).

- *Mr. Davison was correct when he observed that just about every American knows that it costs 32 cents to mail a letter or a greeting card. That's why I was a little confused about your suggestion that the economic benefit of bar coding should be available to households. Are you suggesting that the next time I send a birthday card to one of my children I would pay a lower rate if I included a bar code? How would that work?*

My suggestion was oriented towards the future more so than today, but the basic thought is that work that saves the Postal Service money should share in the savings, even if from a household. Approximately one-third of homes today have personal computers and the number is growing all the time. Printers at home allow the automatic generation of addresses on envelopes and will eventually enable individuals to print bar codes as well. To the extent that bar coded envelopes are cheaper for the Postal Service to handle, then the sender should benefit from that savings. A number of people currently use preprinted address labels instead of hand writing or typing the address for a card or letter.

- *When you spoke about the primary focus of the Postal Service, you emphasized that they should be encouraging growth in all categories of its current business. Is it your opinion that the Postal Service should not be allowed to branch out into new product areas?*

This is a complex question. Basically, we believe that the Postal Service should focus on its current core business. However, we recognize that technology and creativity may provide some opportunities for the Postal Service that are very closely related to its mandate and its current business. We understand the appeal of managing a growing organization rather than one that is flat or contracting. On the other hand, we believe the Postal Service must exercise caution as it considers moving into new areas. For example, growth through new areas can be very expensive and sometimes hazardous. More importantly such growth can divert management's attention from its core business.

We suggest that the Postal Service not seek to grow in areas (a) that already are served by multiple competitors, or (b) where the Postal Service does not have a distinctive competence or capability. For example, combining electronic input, creation of mass hard copy output and *physical delivery* of the mail may represent new business opportunities. This type of growth would combine the Service's distinctive capability—*delivery of the mail*—with new technology of electronic input and mass reproduction.

I appreciate the opportunity to provided this additional information. I look forward to continuing participation in this very important process.

Very truly yours,

JACK B. MAYER

RESPONSES TO QUESTIONS FROM JEFF WEISS

AMERICAN GREETINGS,
CLEVELAND, OHIO
March 22,1996

The Honorable Ted Stevens, *Chairman,*
Senate Subcommittee on Post Office and Civil Service
Washington, DC.

DEAR SENATOR STEVENS: Thank you for the opportunity to respond to additional questions. We are pleased to participate in the process.

- *Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?*

No, I don't believe the Postal Service should be free to set rates for non-monopoly services, specifically because there is no sure way to prevent cross-subsidization of the monopoly services once that door is opened.

- *It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?*

  I believe the current structure that establishes the Postal Rate Commission as an independent organization to oversee and review rate and classification changes works very well. As we mentioned in our testimony, we believe the PRC could be even more effective if it had unobstructed access to all the information available at the Postal Service.

- *All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?*

  The Postal Service occupies a unique position today as the only universal delivery entity of hard copy in the country. It should concentrate on improving this core business and becoming a cost efficient and highly productive organization—one that can manage possible volume drops in the future.

- *You are obviously very knowledgeable about the Postal Rate making process and, you have come to the conclusion that not only should the Postal Rate Commission continue its strong oversight function, they should have the additional authority to compel the Postal Service to provide any and all information they may want. Do you envision that the information received by discovery would then be made available to other participants in the process?*

  Yes, I have to believe that the process will be improved overall if everyone in it has as much information as possible.

- *You and Mr. Davison both acknowledge that the Postal Service faces the same challenges as businesses—technology, competition, and changing consumer behavior. Further, you recommend that the Postal Service, as any other business, must reshape and revitalize itself to operate efficiently.*

Do you have any specific suggestions about how the Postal Service can reshape itself to meet the competition aspect of this equation?

What about the changing consumer behavior as it relates to greater use of alternative communications technology?

Of course, this is the difficult question. Cost control is essential. Reduction in size through attrition should be acceptable by labor and management as a real possibility. Hard decisions will have to be made on both sides of the table for improvements to begin to affect the bottom line. If there is some legislative help that can be given to the Postmaster General in the labor management area, it should be done sooner rather than later.

Over time, every organization must reshape itself to meet its new environment. The new shape might be size, composition, capability. The use of new technologies should be planned. The move to fuller automation should be speeded up. Just like all our businesses, the Postal Service must try to be at least one step ahead of changing consumer behavior.

JEFF WEISS

LETTER FROM TIMOTHY J. MAY, COUNSEL FOR THE PARCEL SHIPPERS ASSOCIATION

PATTON BOGGS, LLP
WASHINGTON, DC.
March 29, 1996

The Honorable Ted Stevens, *Chairman*
Subcommittee on Post Office and Civil Service
Committee on Governmental Affairs
U.S. Senate
Washington, DC.

DEAR SENATOR STEVENS: Enclosed are my responses to the questions submitted by your Subcommittee subsequent to my testimony on March 14, 1996. Please forgive the less than prompt response; I have been absent from the city for a week and therefore was unable to attend to this matter until my return.

Please let me know if we can assist the Subcommittee's very valuable efforts in any additional way.

Sincerely yours,

TIMOTHY J. MAY

Enclosure

RESPONSES TO QUESTIONS FROM TIMOTHY J. MAY

Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

It is the position of The Parcel Shippers Association that the Postal Service should be free to set rates, and other service conditions for only some of the non-monopoly services. Specifically, it is our position they should have this freedom for parcel post and express mail. At this time we limit our recommendation to those two services because they are the only two where there is adequate competition in the marketplace to protect consumers who depend upon these services. For example, third-class catalogs are not subject to the postal monopoly, but there is no current marketplace alternative for the delivery of catalogs and thus there would be no protection afforded by the marketplace against unfair or exorbitant prices and services by the Postal Service. It has been our position that, where the Postal Service either has a monopoly or a *de facto* monopoly, the Postal Rate Commission must be involved in the establishment of rates, classifications, and conditions of service, to ensure that the consumers of those services are treated fairly.

In the case of the two services which we recommend be deregulated, parcel post and express mail, as we have noted there is more than adequate competition for parcel post service, primarily from United Parcel Service; and in the case of express mail there are numerous providers of expedited service. The monopoly services would be protected from forced cross-subsidization of parcel post and express mail by empowering the Postal Rate Commission to ensure that the rates and services freely established and negotiated by the Postal Service for those two services fully recover their attributable costs. The Commission would also be empowered to ensure that all similarly situated users of parcel post and express mail were given equal treatment by the Postal Service.

It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?

In addition to the deregulation of parcel post and express mail, the Postal Reorganization Act should be amended in its ratemaking provisions to make clear what we believe the Kappel Commission that studied postal reform, and the Congress that enacted it, intended: that is that, in the determination of the share of overhead borne by classes, due regard is given to modern pricing theory; demand factors should play a significant role in the determination of relative shares of overhead so that the Postal Service would have the needed flexibility in pricing to the market as does any modern business. The refusal of the Postal Rate Commission to give significant weight to demand factors has been criticized by the General Accounting Office.

The three and four year rate cycles should be changed. On the one hand they deprive the Postal Service of flexibility and on the other hand they make the rate increases that are finally implemented larger than they would otherwise be in a shorter time frame. It is not realistic to have rate cases every year and would also be disruptive to have them every two years. Possible changes to be considered include phased rate increases that would phase in over three or four years; or rate flexibility given to the Postal Service to make annual adjustments less than the rate of inflation with omnibus rate proceedings every four or five years to realign costs and rates in a more rational way.

All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?

For those services where the Postal Service currently has or will in the future have direct competition, the Service must have the flexibility to respond to that competition or it will lose not only market share, but it could lose the business altogether. This has already happened in areas where there is direct competition such as parcels and expedited services. Also, if the Postal Service can not achieve pricing that reflects market demand from the Postal Rate Commission, it will lose business where there is no direct competition. An example is third-class letter mail, which is protected by the postal monopoly. To the extent that third-class letter mail becomes unaffordable to direct marketers, they will be compelled to seek alternative means of getting their sales message to their customers. There are means other than the Postal Service to reach those markets, although the Postal Service is the preferred medium. Loss of this kind of business will seriously impair the ability of the Postal Service to continue to perform its public service functions. And, given the climate we operate in, it is unrealistic to expect that there will be future taxpayer support to continue that public service function. Even now, the Congress refuses to pay its share for congresssionally-mandated subsidized non-profit mailings, and has told the for-profit mailers they must make up the loss.

You have suggested that the Postal Service and the Postal Rate Commission agree on some procedural reforms which would result in more efficient consideration of proposals to change rates or classifications, or to establish new products. It was my understanding that this process was ongoing—that the Postal Rate Commission had published for comment some proposed changes requested by the Postal Service. Is my information inaccurate?

Your information that the Postal Rate Commission has published for comment some proposed changes requested by the Postal Service is accurate. However, there are other changes requested by the Postal Service, and asked for by postal customers, that the Commission is not considering at the present time.

You have also recommended that we stop the congressional raids on the USPS pocketbook. First of all, I'd like to go on record as being opposed to treating the Postal Service as a cash cow. However, as a practical matter, it is very difficult to adequately protect an entity which is now off budget and as a result whose "contributions" to deficit reduction are scorable. Do you have any specific suggestions on how this Congress can legally prevent a future Congress from requiring such contributions from the Postal Service?

Your question acknowledges the difficulty of preventing the Congress from taking money from an off budget Postal Service when such "contributions" to the Treasury are scorable for deficit reduction purposes. As we are all aware, it is not possible for a present Congress to prevent a future Congress from doing anything so long as it is not violative of the U.S. Constitution. Of course, if the Postal Service were placed back on budget that would remove all the incentive for future raids on the Postal Service's cash. For a variety of reasons I would not recommend such a course.

One of the most difficult issues facing the Committee is what to do about the present labor/management dysfunction. You are absolutely correct that both sides must share blame. As you know, it is difficult if not impossible to legislate cooperation and culture change. However, in your testimony you alluded to a complicated plan to cause great pain to both management and labor for their failure to reach reasonable accommodations. Would you care to give us the Reader's Digest Condensed Books version, with the permission of our friend from the first panel, Cary Baer (the Reader's Digest witness)?

Your question premises the difficulty of trying to legislate changes in the culture and attitudes of institutions and people that run those institutions. I certainly agree with your statement and agree that it is probably more the reason for the labor/management dysfunction than anything in the law. Strikes are the pain that is caused to both management and labor in the normal marketplace for their failure to agree at the bargaining table. And strikes do cause enormous pain for both sides. While the details could become quite complicated, the objective is to substitute for the pain that strikes would bring with a different form of pain so that both sides have the same incentives that the marketplace normally provides to avoid an impasse in negotiations. (We do not believe that either major postal customers or the American people are prepared to endure a postal strike as a normal procedure to ensure smooth collective bargaining at the Postal Service.) The

answer lies in limiting the ability of the arbitrators to grant awards that do not punish both sides. For example, if the arbitrators were precluded from granting labor awards which were more than 50% of the general inflation rate, that would be very painful to postal labor. Conversely, if the Postal Service were barred by law from recouping the cost of an arbitrator's reward through postal rate increases, that would cause great pain to postal management. Additionally, the arbitrators could be limited so that any award made could last only for a period of one year. The knowledge that the arbitration procedure would be merely a palliative and that the parties would have to return to bargaining within a year might also be a very real incentive to make the system work and to avoid arbitration. Regrettably, there are no pat answers to this question; if there were the private sector would long ago have adopted something other than strikes as a means to settle labor disputes where that can not be achieved at the bargaining table.

LETTER FROM TONDA F. RUSH WITH RESPONSES TO QUESTIONS FROM SENATOR STEVENS INCLUDED

NATIONAL NEWSPAPER ASSOCIATION
ARLINGTON, VIRGINIA
April 11, 1996

Honorable Ted Stevens, *Chairman*
Subcommittee on Post Office and Civil Service
Committee on Governmental Affairs
Senate Office Building
Washington, DC.

DEAR MR. CHAIRMAN: Thank you for submitting the additional questions for our answers.

1. Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

No, the Postal Service must not be free to set rates for "non-monopoly" services. It is important to note that the perception of "non-monopoly" services and the statutory reality differ significantly. For example, the delivery of newspapers and magazines is functionally permitted by the private express statutes, but the Postal Service retains the right under its authorization to change that situation by regulation at its sole discretion. Much of third-class mail is perceived to be "non-monopoly" but in fact is covered by the definition of a letter under the Private Express Statutes.

Regardless of the scope of the monopoly, the Postal Service effectively can cross-subsidize its competitive offerings by maintaining a high level of fixed costs in its accounting system. And, in fact, that is exactly what it does. About 40% of all costs are treated as overhead costs by USPS and that percentage has been rising in recent years.

The only way the public could be protected from cross-subsidization, short of complete oversight authority by the Postal Rate Commission, would be a requirement for separate subsidiaries, without any cost-sharing between the subsidiaries and the parent, for purposes of carrying out competitive services. However, as its carrier costs are presently structured, it is highly doubtful that USPS separate subsidiaries could be low-cost competitors. And, in fact, since it is effectively permitted to control the prices in some so-called competitive markets, the effect of permitting a high-cost subsidiary to enter the market would be to raise the overall prices for consumers.

If the decision were made to free "non-monoply" rates from regulatory oversight, then the minimum statutory requirement should be to require that the unregulated rates fully cover costs and make a contribution to institutional overhead at least equal to the system-wide average that regulated rates make to cover fixed costs.

2. It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body in a modernized Postal Service. What specific changes would you make to the current structure?

We would recommend subpoena power for the Postal Rate Commission as to all USPS cost and revenue records. We would also recommend final rate

authority for the Commission, subject to de novo review by the courts and authority for the Postal Rate Commission to represent itself in these suits.

It is our view that every single one of the 8,000 newspapers in the United States—except the Wall Street Journal—would vehemently object to any "postal reform" bill that would not expand and enhance the powers of the Postal Rate Commission. The Postal Service has already clearly stated its intentions for periodicals. It wants to give a 14 percent rate reduction for 250 large, national periodicals and a 17 percent rate increase for the 12,000 smaller periodicals.

Because of the unique nature of the subject matter of postal rate making there must be some insurance that the regulatory body has the expertise, institutional memory and proper tools to analyze the Postal Service in an effective way. We are concerned about current down-sizing efforts at the Commission. We recognize the staff reductions have been taken voluntarily by the PRC, but it needs trained staff available when a rate case is submitted.

3. All of our witnesses agree that the Postal Service must continue into the next century'. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?

Yes, we really do need a strong Postal Service into the far distant future. Most community newspapers are dependent on the Postal Service for delivery now and as far into the future as we can reasonably predict.

On the other hand, it is doubtful that USPS can forestall the realities of the marketplace, which increasingly favors businesses with low fixed costs, high flexibility and manageable labor expenses.

The Postal Service already offers lower rates for volume mailers and high density mail. In doing so it favors larger publications at the expense of small publications. The current structure also discriminates against rural areas and inner city ZIP codes. For example, Alaska has about four times as many ZIP codes as Los Angeles but only one-twentieth the population. There is no mathematical way that volume and density in Alaska can qualify for the same lower rates that Los Angeles can enjoy. This is why rural residents receive fewer pieces of mail on average each day.

The same problem is true with less affluent inner-city ZIP codes. Attachment A to these questions is a recent article from DM News noting that African Americans receive 80 percent fewer catalogs than whites.

For the Postal Service to try to avoid the consequences by utilizing a business plan that requires growing volume for volume's sake, regardless of the effect upon the private sector or competitors or the impact of new technologies on communications, is entirely foolish. As Congress and USPS management seek the formula for bringing the Postal Service into the 21st Century, it is important to recognize that the origin of the problem is not in rate regulation nor inflexible oversight, but in the structure of USPS. More than likely, the key to the future is in planned and carefully engineered restructuring and possibly some downsizing.

The entirely implausible idea that J.C. Penney would turn $1 billion worth of parcel business over to the Postal Service is pretty farfetched. No other American business has come close to making such a commitment and, of course, for the Postal Service to give J.C. Penney a rate decrease in exchange for its business would result in a rate increase to all other parcel shippers.

A discount for J.C. Penney would be harmful to newspapers. Our advertisers are primarily local retailers whose advertising budgets are based on gross sales. When someone from Wasilla, Alaska buys a parka by mail from J.C. Penney, the newspaper in Wasilla loses a little advertising business and the community loses some sales tax. At least UPS pays property taxes and motor vehicle taxes in Alaska—unlike the Postal Service.

We would strongly urge the Subcommittee to invite Bill McCarthy, head of J.C. Penney's catalog division, to testify in public on his conversation with Marvin Runyon and why he would prefer to do business with USPS rather than UPS. His testimony could also help outline the impact a favored rate

for his company would have on other parcel shippers who were not covered by a sweetheart rate.

4. I noted in your testimony that having a monopoly and a universal service requirement means that no one will be singled out for better or worse treatment with regard to postage rates. However, as you know, the monopoly applies only to letter mail. Some have suggested that the Postal Service be granted pricing flexibilities for non-monopoly services. Would your members object to pricing flexibilities for non-monopoly services?

Our members are one-hundred percent against "pricing flexibilities" for non-monopoly services. Again, the definition of a "letter" and the scope of the postal monopoly are widely misunderstood. Under the current rules, both a newspaper and a flat advertising piece may be considered letters. If "pricing flexibility" for "non-letter mail" includes a new power for the Postal Service to run rampant through the advertising marketplace, our association would most assuredly object. Furthermore, "pricing flexibilities" are counter to the long-run interests of the Postal Service. In the recent reclassification case, Time-Warner received about a $10 million reduction in its postage rates. Nevertheless, it still has the same number of subscribers it is serving and it seems unlikely the Postal Service will pick up any new business from that $10 million price reduction.

5. I also noted your comment that the biggest problem with volume discounts and contract rates is that the Postal Service has no profits to absorb lower rates for some customers and that, as a result, other customers will be required to pay more. In your opinion, is there a way for the Postal Service to be allowed to earn a small profit to prevent this problem?

If the Postal Service were to be completely privatized so that it could absorb all of the risks and privileges of a private sector business, it could legitimately earn profits. But it should not be permitted to use its retained earnings to subsidize some customers while also regulating its competitors and claiming sovereign immunity for non-performance. That would be the worst of both worlds for both the consumer and the private sector competitors.

Attachment B to these questions is a speech by the Postmaster General in which he notes that American business has seen a two percent increase in productivity in the last two years while Postal Service productivity has fallen two percent. The Postal Service cannot reasonably compete in any arena with its uncontrolled costs and falling productivity.

6. The examples you cited to show the importance of the Postal Rate Commission to your members serves to also reinforce at least additional problems—the high cost of participation in this process and the need for the Postal Service to develop and maintain systems which can provide accurate information.

In your opinion, is there a way to not only streamline the current regulatory system but decrease the attendant cost to participants?

In your opinion, is the Postal Service working to develop the necessary systems to be able to provide accurate information?

Our association accepts the cost of litigation before the PRC as a necessary component of maintaining the Postal Service's public service mission and its attendant regulatory status. Our problem comes when quibbling over data that in any other regulated industry would be public record and/or subject to subpoena. But because of the Postal Service's heightened sensitivity to its competitive status, it is often overzealous, in our view, in protecting data that are pertinent to the public service mission. This is another example of the neither-fish-nor-fowl predicament in which USPS finds itself by virtue of its statutory mandates.

We believe the Postal Rate Commission bends over backwards to be fair to USPS. In fact, at times we fear that in its vigilance not to be too heavy handed in regulation, it fails to recognize its equal obligation to the private sector marketplace. In fact, it should not be the overriding obligation of either the PRC nor the Congress to keep the Postal Service in business if and when it becomes apparent that private sector alternatives are superior in cost and service. The ultimate obligation of both must be to the public interest and not to the captive interests of any agency or portfolio under their jurisdiction.

Because the regulatory process at the Commission is the fastest of any agency in Washington, the speed of the process contributes to some additional expenses and we would oppose requiring the Commission to operate even faster. The Postal Service has an overwhelming advantage in this environment.

Finally, it is important to keep in mind that the United States is undergoing an unprecedented revolution in communications. No amount of rate reduction or service performance or cost control on the part of the Postal Service will change the direction we are heading. The very best goal for the Postal Service's long-term well-being is to do what it is doing now as capably and efficiently and as cheaply as it possibly can.

Sincerely,

TONDA F. RUSH
President and CEO

ATTACHMENT A—DM NEWS ARTICLE DATED MARCH 4, 1996

BLACKS RECEIVE 80% FEWER CATALOGS THAN WHITES

DMers advised to look at similarities in tastes, not differences

BY SUZANNE E. GALLAGHER

NEW YORK—The African American and Asian American markets—which together have about $500 billion in purchasing power—are virtually untapped by direct marketers, according to experts speaking at the DMA's first Multicultural Marketing Day here last week.

Even though African Americans together represent $350 billion in purchasing power, the average black household receives 80 percent fewer catalogs than the average white household.

"I think there's a lot of stereotypes with this market: If it's not black or black-related they don't want it," said Cheryl Loorkhoor, a list manager at the Kleid Co., which has databases of three lists with more than 250,000 African American names. "They believe we only want what's created for us."

Conceding that the African American consumer market is different in some ways from the general market, Loorkhoor pointed out that they want the same products—apparel, furnishings, financial services and entertainment. In other words, direct marketers would do best to "look at similarities, not differences," she said.

The biggest obstacle is finding and renting buyer lists that identify blacks. "You can't go into a non-white area, eliminate non-blacks and then assume that the rest are black," she said.

Her suggestions: Use files from African American magazines, specialty catalogs, TV-generated lists, ticket buyers' lists and other cultural events. In addition, she said, marketers should develop relationships with black colleges, especially sororities and fraternities; create strategic alliances with African American organizations, and attend relevant conventions and gatherings.

Robert Acquaye, director of circulation at black Enterprise magazine, suggested building lists through partnerships with churches and other neighborhood organizations.

The most important point to keep in mind is that blacks are as diverse as any other racial or ethnic group. To make effective appeals, marketers need to pay attention to different segments of the market, research it and learn about African American interests and concerns, Loorkhoor said.

Some facts to keep in mind: Sixty percent of African Americans have children; most are single parents. The majority live in the southeast, 82 percent in a metropolitan area.

Another large population neglected by direct marketers is Asian Americans, a group that's expected to reach 38 million people by the year 2050, five times what it was it 1990.

When trying to reach this group, Cindy Lin, a list manager at Database Management, suggested that marketers keep in mind the many cultures that come under that single banner. Approximately 24 percent of Asian Americans are of Chinese descent, followed by Filipinos at 20 percent, Japanese at 12 percent, Asian Indians at 11.8 percent, Koreans at 11.6 percent and Vietnamese at 8.9 percent.

Most Asian Americans speak their native tongue at home, with the exception of Japanese households, which tend to use more English, said Lin. The average Asian

American household size is 3.8 people, above the 2.6 average of the general population.

Historically, the Asian American response rate to direct mail has been triple that of the general population. But, to be effective, direct mail pieces must be bilingual, she said. Unfortunately, buying lists are scarce and 95 percent of those available are geographic files based solely on surnames picked out of phone books in areas where Asians live in high concentrations.

ATTACHMENT B—POSTAL NEWS ARTICLE DATED FEBRUARY 28, 1996

REMARKS BY POSTMASTER GENERAL MARVIN RUNYON BEFORE THE NATIONAL LEAGUE OF POSTMASTERS LEGISLATIVE CONFERENCE, ARLINGTON, VA

I want to thank all of you for your hospitality last night. I really enjoyed myself, and I appreciate the opportunity to spend some time with you.

This morning, I want to talk candidly with you about our future, both its promise and its uncertainty. And I want to share with you what it is going to take to make it strong and secure.

As I look to our future, I see a great deal of potential. The Postal Service has an important mission. We serve everyone, everywhere, every day, delivering communications value to the nation. And thanks to you, we are making history for our customers. We have provided four years of stable rates for the first time in 25 years. We have taken overnight service performance from the low 80's to nearly 90. And we have done it while making more money than ever before.

We couldn't have done that without all of you. You and your fellow postmasters and supervisors have worked hard to help us get to where we are today. You have done an outstanding job.

At the same time, though, I have some serious concerns about our future. I am here to tell you, we face a real uphill battle in the days to come.

There are three reasons why I feel that way. The first is how tough our competition is becoming. Even though we are moving steadily forward in out performance, our competitors are beating us, and beating us pretty soundly, in just about every area of our business. Their service is better. Their overall value is better. And they are doing a better job of winning customers than we are.

All of this is taking its toll. Of our six major product areas, from correspondence to publications, we are losing out in all but one. So far in 1996, mail volume is down 730 million pieces. It was off during our first quarter, which is our heaviest mailing season. And it is down in the second quarter as well. For a company that has doubled its volume every twenty years, this is bad news indeed.

The second reason that we have an uphill fight is because of changes in the marketplace. Other companies are cutting their costs to stay in business. And that is costing us business.

Let me give you a prime example. Nearly one out of every four mail pieces we get is either a bill, a payment, or a statement. Today, that part of our business is under serious attack. Big corporations like Wal-Mart are *requiring* the companies they deal with to send them invoices and statements electronically, rather than through the mail. I can't blame them. It saves time and money and makes good business sense for them.

Banks are also going electronic. It is not a matter of if, but when. Take Citibank. With their new service, you can use your home computer to pay your bills, review your account balances, and see if your checks cleared—all for free. As they say in their full-page ad, "No checks, no stamps, no envelopes." What it really says is "No mail."

These services are catching on with customers. In six years, we have lost $2 billion in potential business. By the end of the century, a third of all consumers say they will stop using the mail to pay their bills. Because of electronics, a quarter of our business today is up for grabs.

Third, there is no costs. Over the last ten years, our work hours have grown 15 percent. That is understandable considering the growth in volume. But the cost of those work hours has grown three times as fast. And it is eating away at our profits. The $1.8 billion net income we made last year will shrink to just $500 million this year because of rising cots, most of it salaries and benefits. By the year 2000, total expenses will rise $14 billion. That is $14 billion we will have to make up in sales and lower costs just to stay even.

Rising costs, shrinking volume, declining market share . . . no business can run that way for long. We won't either. If we do nothing, we will have no choice but to pass our rising costs on to our customers. When we raise prices, they will take

their business elsewhere. And you know as well as I do, rising rates and falling volume are a sure-fire way to go out of business quickly.

I don't want to see that happen. I want this company to be successful. I know you do, too. We are both working hard every day for this organization. But the bottom line is this: Our best has got to get better.

I am convinced that we must act, and act now, to get ahead of the curve. We have got to move our strategies forward faster than we had planned. And we must act boldly. To succeed, it is going to take some fundamental changes in the way we do things.

Earlier this month, the Officers met to look at the 1997 budget. Forecasts called for us to lose $652 million. That was unacceptable. So the Officers agreed to new programs to add more than $750 million to our bottom line. As a result, I was able to tell the Governors at our February meeting that we will make a $100 million net income next year. But that will enable us to hold postage rates stable only through 1997. That is not good enough. We have got to do everything we can to keep stamp prices steady until the next century. If we don't hold down prices, we simply won't hold on to our customers.

We also must have better service. This year, our CustomerPerfect. goal is to get on-time delivery of First-Class Mail up to 90 percent nationwide in Quarters III and IV. By the year 2000, we need to reach a national overnight average of 95 percent. And that is just to keep us close to our competitors.

Stable rates until the next century, service scores at 95 percent by the year 2000, why these tough goals? Because steady prices and better service are what the customers want. They are the difference between winning the business, or going out of business. Just ask the customer. Nine out of ten said they would continue to bring us their business, and three out of ten will bring us more, but only if we improve service and keep prices low.

We can do it. We can reach these goals and stay in the race. We have got the talent. It is here in front of me.

Let me tell you what it is going to take to succeed. First, we have got to get serious about winning customers and finding new sources of revenue. Second, we have got to find new ways to control our costs. And third, we have got to constantly improve our productivity—doing more, doing it faster, and doing it with less.

Let's talk about them one-by-one.

First, building the business. I want us to bring in an extra $1 billion each year through new and better postal products and services. We are working on it. We are testing new services that take advantage of our existing network, things like FastNet, Pack-and-Send, and phone cards. We are developing a range of financial services, including one that lets customers send money by wire from our post offices. We are building new postal stores at the rate of one per day, to help us look more like a department store and less like a waiting room. We are beginning to test new electronic products. And we are going to beef up our presence in profitable markets. For example, we are creating a separate mail stream for Priority Mail so we can push on-time delivery into the high 90s. And we are taking it around the world, as Global Priority Mail.

We are also asking Congress to give us the freedom to run the Postal Service like a business, so we can win back our customers' business. We have told Congress that we are trying to compete with one hand tied behind our back, in the worst of all worlds—tough private sector competition and burdensome government regulation.

It has cost us plenty. We have lost big contracts with big customers. The federal government sends it expedited mail not with us, but with FedEx. Last July, J.C. Penney made national news by signing a contract with UPS to deliver its packages for one billion dollars. The loser? The Postal Service. Because the law won't let us offer the volume discounts that J.C. Penney needs. Bill McCarthy, head of J.C. Penney's catalog division, told me, "Marvin, if the Postal Service had just some of the freedoms that UPS enjoys, we would *not* have signed that UPS. We would have rather given that business to the Postal Service."

I am going to do everything I can to help us get those freedoms in the next three years. And I will be calling on you to pitch in, too. I need you to be involved in this process. Your voice is stronger, your influence greater. When postmasters talk, people listen.

The second thing we must do is cut our costs. To hold off a rate increase until the year 2000, we have got to make up a total of $12.4 billion. We are already working to close that gap. We are working on 17 different projects to use technology to reduce costs, from robotics that will load mail from trays onto pallets to a new low-cost OCR. In large plants, we are focusing on reducing overtime and taking better advantage of workforce flexibility with a new computer scheduling system. We are identifying new ways to reduce the cost of workers' compensation. We are develop-

ing a new information system that will enable us to make sure every transportation dollar is used effectively. And we are going to give you point-of-sale electronics to help you have the right products in stock when the customers want them, and tell you instantly how much money you are taking in.

We have also got to take a hard look at contracting out. Our core strength is delivering the mail. When it comes to cutting costs, everything else is on the table. There are a lot of people out there who can do some of our work better and cheaper. For some, this will be a bitter pill to swallow. But we have all got to realize, if we don't control our costs, one day *none of us* will have jobs.

Third, we have got to get better each day. All great companies do. Our productivity increases have been minimal over the last ten years, a total of about three-and-a-half percent. In the last two years, private sector productivity has increased two percent, while ours has fallen two percent.

We have got to get better to stay competitive. I would like to see us improve productivity at least two percent every year, saving $1 billion annually. To get there, we must work to make the most of new technology. Classification reform will help, by encouraging mailers to automate more of their mailings and their systems.

We must also put CustomerPerfect. in place throughout the Postal Service. CustomerPerfect. is more than just words. It is the way we are going to do business from top to bottom in this organization. In the long run, it will create new ways to do your jobs, and give you better information so you can make better decisions. CustomerPerfect. will work, if you make it work.

These are important efforts, but they are only part of the answer. I am counting on you to deliver excellence and new ideas. You are the most important person in the Postal Service when it comes to winning and keeping customers, controlling costs, and increasing our productivity. Each of you is the Chief Operating Officer for your post office. I rely on you to know and manage every detail of your operation, from safety to staffing. The efforts you make is keeping overtime down, adjusting your mix of staffing, and ensuring that your automation pays for itself are critical to our success.

You are also the key to your employees' success. They look to you for information about what is happening in the Postal Service, and what is expected of them. Keep them informed on the local cluster, area, and national goals. Help them understand how they fit in, and what they can do to help.

When it comes to customers, I need you to do your best to deliver on their expectations. Put our best foot forward by maintaining a positive, professional image, from the way our employees dress to the neatness of our vehicles and lobbies. If you have a large mailing from a big customer, let them know that you have gotten their mail out on time. It will reassure them that you care about their business. And as always, be on the look out for opportunities to sell our products. A little effort can go a long way. Like Roger Nadeau, the postmaster of Lewiston, Maine. Roger took the time to talk to a local company about the value of Priority Mail. He turned a million-dollar customer for UPS into a million-dollar customer for the USPS.

With your help, we can reach our goals. We can beat the competition, and win back our business. But we have got to deliver our best. If we demand excellence of ourselves, we will deliver excellence to our customers.

I want to close with a story about a tightrope walker who decided to cross Niagara Falls. Nobody believed he could do it, and a crowd gathered to watch. But to everyone's amazement, he made it safely across, and they all cheered. Then he asked the crowd, "Who believes I can do it blindfolded?" Again they shouted for him not to try. But sure enough, he made it across with ease. Then the guy on the high wire said, "Who thinks I can ride across on a bicycle?" No one thought he could, but once again, he proved them wrong. Finally, he asked, "Who believes I can push a loaded wheelbarrow across?" And they all shouted, "We do, we do." The guy on the high wire smiled and said, "Great. Now, who wants to come along for the ride?"

It is time for everyone in the Postal Service to summon up their courage. It is time to get out there on the high wire and make believers out of our customers. I am confident that together, we can do just that. We can be the leader in our industry. We can provide quality and value that are second-to-one. We can hold our heads high, and come to work every day proud of what we do for this nation. We know what we need to do. Let's make it happen.

I would like to leave you with a story that sums up all that I have talked about today. Remember the alternate delivery company called Publishers Express? They came on the scene a few years back with a lot of fanfare and tough talk. They said they were going to deliver magazines and advertisements faster and cheaper than us. Eleven days ago, they quietly went out of business. They said that they were

no longer needed. They had no more customers. They went out of business, because we improved service and kept costs low.

I can't say that I am sorry to see them go. But they taught us two valuable lessons. First, if we don't do our jobs, somebody else will. And second, when we get our act together, we can be one hell of a competitor.

LETTER FROM JOHN F. STURM WITH RESPONSES TO QUESTIONS FROM SENATOR STEVENS

NEWSPAPER ASSOCIATION OF AMERICA,
RESTON, VIRGINIA,
March 28, 1996

The Honorable Ted Stevens, *Chairman,*
Subcommittee on the Post Office and Civil Service
Committee on Government Affairs
Senate Hart Office Building
Washington, DC.

DEAR CHAIRMAN STEVENS: Thank you for giving me the opportunity on March 14, 1996, to share with you our industry's views on postal reform matters.

NAA commends you for the careful and deliberative approach that you have taken in examining postal service in this country. We encourage you to continue in this manner when considering proposals to change the postal system, for it is our view that any change in the postal system, small or large, will have an effect on mail services and costs for every American citizen.

Attached are our responses to the questions that you posed to us for the hearing record. We would be pleased to visit with you and your staff to expand further on our answers if you wish.

Thank you again, Mr. Chairman, for seeking out and listening to the views of the newspaper industry on this most important issue.

Sincerely,

JOHN F. STURM,
President and Chief Executive Officer

RESPONSE OF THE NEWSPAPER ASSOCIATION OF AMERICA TO QUESTIONS POSED BY CHAIRMAN STEVENS, FOLLOWING MR. STURM'S TESTIMONY OF MARCH 14, 1996.

Question 1. Should the Postal Service be free to set rates for non-monopoly services? If so, how do we protect the monopoly services from forced cross-subsidization?

No, the Postal Service should not be free to set rates for non-monopoly services.

For everyone who would get a rate decrease, someone else would get a rate increase. Those getting rate decreases would be getting them only because the Postal Service has a group of monopoly mailers onto which it can shift the costs, safe in the knowledge that this group cannot leave the postal system for less expensive alternatives without risking substantial civil and criminal liability. We believe this is wrong and fundamentally at odds with the concept of a postal system devoted to the public service.

Today, First Class bears a disproportionate burden of the overhead of the Postal Service. While First Class makes up 54 percent of the volume of the Postal Service, it bears 76 percent of the overhead costs of the entire system.[1] Allowing the Postal Service to set its own non-monopoly rates would place an even higher overhead cost burden on First Class mail.

Some may argue that lower rates set outside of the regulatory framework would bring increased volumes and increased contribution to overhead (institutional) costs. While that might be true for any group of mail that has "elastic" demand in the economic sense of the term, that is not true for any group of mail that is "inelastic". *All mail classes, except for Express Mail, are "inelastic," according to the Postal Service's own data and own econo-*

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[1] This skew is *not* related in any way to the costs of First Class, or those of any other class of mail.

mists. This means that increasing volumes by lowering rates in any service, except Express Mail, will not increase contribution to institutional costs. Volume increases that do not increase the net contribution to institutional costs, and thus do not support universal service, are of no benefit to the general mailing public and the system overall.

Question 2. It appears that all of our witnesses agree that there is a function for the Postal Rate Commission, or some regulatory body, in a modernized Postal Service. What specific changes would you make to the current structure?

First, give the Postal Rate Commission final rate-setting authority.

Second, give it subpoena power over the Postal Service, so that it may obtain the data it needs to do its job.

Third, allow the Commission to represent itself in court. Today, if the Postal Service loses an issue before the Commission, and there is an appeal, it is the Postal Service that "defends" the Rate Commission rejection of their position before the appellate court. This makes no sense whatever.[2]

Fourth, the committee might want to consider giving the PRC the authority to set the Postal Service's revenue requirement. If the Commission had full authority over the requirement, the Postal Service would truly have to grant the Commission full access to all it's data. Moreover, the current system, which leaves revenue requirement decisions solely to the governors, has not successfully achieved the statutory objectives that rates should cover costs. This is evident by the fact that the Postal Service has lost some $9 billion since reorganization and currently has a negative net equity position.

Question 3. All of our witnesses agree that the Postal Service must continue into the next century. If the Postal Service is not given the tools to compete in the marketplace, how will they be able to continue the basic public service function without taxpayer support?

We believe there is no complementary relationship between "competing in the marketplace" and continuing the basic public service function of the postal system. The two are fundamentally different and contradictory goals. Reshaping the Postal Service into a government institution that competes with the private sector will by definition orient it away from its current public service mission. Moreover, to the degree that the postal service has problems with losing any mail to "competition," the problem is costs, not rates.

Question 4. You stated that the Postal Service you envision would remain a public service devoted to universal and nondiscriminatory service. Exactly what do you mean by nondiscriminatory?

If one of our member's mail pieces costs ten cents for the Postal Service to deliver, and a competitor's piece that is just like it also costs ten cents for the Postal Service to deliver, then the Postal Service should not be allowed to discriminate between the two and charge different prices. Under no circumstances should one of them be allowed to pay less than the other.

Under a contract rate, volume discount, or pricing flexibility theory, if one of our member's competitors were part of a large national mailing company, then the Postal Service could allow that competitor to pay less than our member, based upon a national contract, even though both of our pieces costs exactly the same for the Service to process and deliver. This is discriminatory pricing and has no place in our postal system.

Postal Services are a fundamental government service, and should be available to the public at nondiscriminatory prices.

Question 5. As I have stated before, I am not sure that the Postal Service is broken and needs a major fix. However, I do believe that it is necessary to fine-tune its operations in order for it to survive to provide universal delivery service to every corner of our country into the next century—something that seems to be important to all mailers. In your opinion, are any of the flexibilities which have been suggested this morning acceptable to the Newspaper Association of America?

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[2] It is this flaw in the current law that in 1992 prompted a federal district court to enjoin President Bush from dismissing the Postmaster General and several governors for refusing to withdraw a brief that patently refused to defend the Commission.

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We would support reasonable proposals that go toward the operational flexibility of the Postal Service, particularly proposals that would help the Postal Service control its costs and make itself more productive and efficient.

We would vigorously oppose any proposal that promotes pricing discrimination (euphemistically called "pricing flexibility" by USPS).

Changing the pricing mechanism of the Postal Service would be much more than a major change to the institution, it would be a radical change; and a radical change that was opposed by almost two-thirds of the groups that testified before the subcommittee.

It is important to remember that, in our view, the Postal Service's challenges are in dealing with its costs first. The focus of the Service should be to cut costs, not deals.

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